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July 4, 2013

U.S. Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549

Re: JOBS Act Title III SEC Regulatory Rulemaking

Ladies and Gentlemen:

City First Enterprises appreciates the opportunity to comment and share our views on the SEC's Regulatory Initiatives under Title III of the Jumpstart Our Business Startups Act (JOBS Act).

In April 2012, Congress passed the JOBS Act, including Title III also known as the CROWDFUND Act, which creates a new exemption from registration of securities sold via crowdfunding when certain criteria are met. The SEC is charged with developing rules that achieve the legislation's intent of facilitating job-creating capital formation while protecting investors. We believe there is an opportunity to responsibly balance crowdfunded capital formation in disinvested communities with strong investor protections. This letter outlines a solution to do so at scale while creating an orderly, transparent, and efficient marketplace for mission-driven securities crowdfunding.

I. Overview

Our objective is to ensure that the law's core intended outcome of job creation extends to underinvested, low-income communities, where unemployment is high and jobs are needed most. This section outlines the opportunity, potential challenges, and a solution that will increase job-creating mission capital formation while enhancing investor protections.

A. Mission Investors, the CROWDFUND Act and Job Creation

Mission investors, those driven to invest primarily by charitable motivations, could substantially contribute to the law's intent of channeling new capital towards the creation of jobs, particularly in low-income communities and among populations with high levels of unemployment.¹ While we are enthusiastic about

¹ Individuals who engage in mission investing also engage in profit maximizing investing, although typically display different investment behavior based on the type of investment. Most notably, when making mission investments, investors exhibit a willingness to accept lower rates of financial return when an investment helps achieve other, charitable objectives. For those investors engaging in mission investing, which may also be referred to as "impact investing," the mission portion of their portfolio and average investment size tend to be small. See, e.g. J. P. Morgan "Impact Investments—An emerging asset class." *Rockefeller Foundation and Global Impact Investor Network* (2010). Pages 30-38.

the ability of securities crowdfunding to generate new capital for underserved communities, we also believe that there is a risk that certain implementing rules may inhibit mission investor participation and thus severely limit the job creating potential of the legislation in communities with high levels of unemployment. As detailed below, anticipated investor protection mechanisms in the forthcoming rules may create barriers that will prevent participation by mission investors.

We recognize that it is necessary for the SEC to develop rules that strike a balance between capital formation and investor protection. We write to support and detail an already-introduced² solution that will provide an alternative set of investor protections stronger than those called for in the law that would avoid otherwise-anticipated barriers to mission investor participation. By leveraging the national reach and expertise of Community Development Financial Institutions (CDFIs), the proposed rules for mission investors will establish an orderly, efficient marketplace that facilitates the formation of mission-driven capital at scale while enhancing the quality of investments offered.

B. Crowdfunding and the Opportunity of CDFI-Facilitated Mission Capital Formation

CDFIs are private, federally-accredited providers of mission finance. CDFIs have an unparalleled track record of providing responsible, affordable financing that creates jobs and drives economic development in underinvested communities.³

Inadequate access to capital is a major impediment to CDFIs achieving even greater job creation and community impact. CDFI-financed transactions frequently suffer from a lack of “gap” financing, which is the shortfall between the amount of a business’s equity in the project and the amount that the CDFI is able to finance. At the same time, there are currently no efficient ways for small-dollar mission investors to invest in community businesses. Mission-driven crowdfunding represents a solution to this problem, enabling the flow of mission capital to CDFI transactions, filling financing gaps and enabling more mission transactions to come together. The result will be a significant new marketplace for responsibly channeling capital that generates jobs and economic development where the U.S. economy needs it most.

With more than 1,000 CDFIs already originating approximately \$6 billion a year in mission finance,⁴ CDFIs are well positioned to responsibly facilitate crowdfunded mission capital formation. They will be able to use their established networks and financial expertise to efficiently direct mission investments from crowdfunding investors to underserved communities.

C. The Challenge within the CROWDFUND Act and a Solution

As noted above, there is a risk that the rules to implement the CROWDFUND Act could stifle this opportunity. There are two primary concerns for CDFIs. First, income and/or asset verification for mission investors who

² Senator Jeff Merkley (OR). "Crowdfunding." *Congressional Record* 158:113 (July 26, 2012) page S5474.

³ See below Sections II. C.-E., page 7.

⁴ See e.g., "Industry Statistics." *Opportunity Finance Network*. Page 1. <<https://www.opportunityfinance.net/industry/default.aspx?id=234>>. Industry wide data is collected by the CDFI Data Project (CDP), a CDFI industry collaborative. The CDP collected data on 495 CDFIs in FY 2008.

will typically seek to invest very small amounts may prove overly burdensome. Second, marketing limitations may limit the ability to inform these investors of mission investment opportunities.

In response to this concern, we propose and detail a regime that includes robust investor protection mechanisms based on CDFIs' strong investment experience, financial soundness and credibility. The regime will be centered around a new type of crowdfunding portal called a CDFI Jobs Portal. In the context of this stronger investor protection regime facilitated by CDFI Jobs Portals for investments in the public interest, we recommend (i) simpler standards that minimize barriers to making small mission investments, and (ii) clarifying marketing rules for CDFI Jobs Portals consistent with what is permitted under the Act. In this way, the proposed implementing rules⁵ would promote, rather than stifle, the mission capital formation opportunity while ensuring investor protection.

D. Outline of CDFI Jobs Portal Requirements, Supplementary Investor Protections and Permissions

The central purpose of the CDFI Jobs Portal is to provide a neutral platform for other CDFIs and enterprises in low-income communities to responsibly attract mission capital to their transactions in a way that protects investors from fraud and substantially mitigates investment risk. To make possible these implementing rules encouraging mission investor participation – rules that allow fewer personal disclosures and marketing of mission impact – CDFI Jobs Portals and their participants would be subject to a series of supplementary investor protections more stringent than those required by the law, including:

Requirements of CDFI Jobs Portals

CDFI Jobs Portals must be operated or controlled by entities that meet three criteria: they must be (i) federally-regulated financial institutions that are also (ii) public charities and (iii) certified CDFIs.⁶

- *Regulated Financial Institution Requirement:* Each CDFI Jobs Portal will be subject to supplementary and independent regulatory oversight by a federal banking regulator, ensuring safety and soundness as well as financial stability of the operating entity.
- *Public Charity Requirement:* Each entity operating a CDFI Jobs Portal must also be a charity, and thus accountable to the Internal Revenue Service for pursuing charitable impact.
- *Certified CDFI Requirement:* Entities operating CDFI Jobs Portals must be certified as Community Development Financial Institutions by the U.S. Treasury Department's CDFI Fund, which only certifies entities with a proven track record in community development finance.

Investor Protection Requirements Implemented by CDFI Jobs Portals

CDFI Jobs Portals must implement a series of strong investor protections that would not be required of other funding portals.

⁵ See Appendix A.

⁶ The number of Federally Regulated 501(c)(3) Certified CDFIs is quite small, so the SEC would not need to be concerned with a large marketplace of CDFI Jobs Portals to oversee. As a result, the regulatory burden of overseeing CDFI Jobs Portals will be minimal.

- *Sophisticated CDFI Co-Investor Requirement:* In order to post an offering on a CDFI Jobs Portal, an issuer must have attracted a co-investment from a qualified CDFI in the same transaction.
- *CDFI Co-Investor Performance Standards Requirement:* To qualify as a participating co-investor on a CDFI Jobs Portal, CDFIs must meet high performance standards relating to loan loss rates, reserves, and capitalization.
- *Issuer First-Loss Requirement:* Each issuer must invest or put at risk its own resources in order to be eligible for a crowdfunding investment through a CDFI Jobs Portal.
- *Low-Return Debt Requirement:* Offerings on CDFI Jobs Portals will be restricted to low-yield⁷ debt securities, thereby eliminating the “get-rich-quick” temptation some investors may have and attracting investors who are motivated more by mission impact of the offering than by its potential outsized financial return.
- *Privacy Protection Requirement:* Like all crowdfunding portals, CDFI Jobs Portals will collect sensitive personal financial information. Because CDFI Jobs Portals must be controlled by regulated financial institutions, they will be subject to Gramm-Leach-Bliley privacy rules, thereby easily meeting the privacy protection mandate in the CROWDFUND Act.

Permission for CDFI Jobs Portals

We believe this series of requirements, taken together, creates an investor protection regime stronger than that required under the CROWDFUND Act. We feel the strength of this regime justifies income and/or asset verification and marketing standards that accommodate small-dollar mission capital formation. Specifically, we recommend that the SEC:

- *Minimize Personal Disclosure Barriers to Participation:* Exempt investors from significant data disclosure requirements for aggregate investments below \$500 on CDFI Jobs Portals (or, in the alternative, a low-threshold “check-the-box” verification solution).
- *Permit Marketing of Mission Impact:* Allow CDFI Jobs Portals and issuers to market the projected non-financial, mission-impact elements of posted offerings. To date, successful non-securities crowdfunding efforts have relied on marketing to attract passionate supporters. Low-return mission investments are analogous to this passion-driven format. We believe that permitting marketing of mission elements would not conflict with the law’s restriction on advertising terms, as we do not believe mission elements of the transaction constitute “terms of the offering”.⁸

⁷ Offering annual interest rates no higher than 5%.

⁸ We do not believe mission elements of the transaction constitute “terms of the offering” per Securities Act of 1933, Section 4A (b)(1)(H)(2).

- *Minimize Any Other Potential Barriers:* Given the supplementary investor protections described above and CDFIs' service of the public interest, we request that the SEC exempt CDFI Jobs Portals from any other rules that might limit their charitable and job-creating impact.

It is our belief that this relief will provide the SEC and the crowdfunding industry with useful experience to advance the long-term growth of crowdfunding generally. The experience and ultimate effectiveness of this approach provide a secure way for the SEC to expand access to crowdfunding for mission impact while potentially informing the SEC's future rulemaking around crowdfunding more broadly.

E. Relevant Precedent for Exemptive Relief

Since their inception, the federal securities laws and the SEC have provided broad exemptions for public charities and benevolent organizations because they serve the public interest.⁹ These broad exemptions make it simpler for individuals to invest for the public good. They also make it easier and less costly for resource-limited charitable enterprises to access capital for mission impact. This proposal enables the SEC to apply to the Title III rulemaking its long-standing recognition of the unique nature of offerings that serve the public interest.

F. This Letter

In this letter we detail the strong and established track record of CDFIs in providing responsible capital that grows businesses, creates jobs, and advances economic development in low-income communities that are otherwise financially underserved. We then outline the potential of the CROWDFUND Act to facilitate mission capital formation that would present a new and substantial source of capital in these communities.

The remainder of this letter follows the structure of economic regulatory analysis described in the Commission memorandum "Current Guidance on Economic Analysis in SEC Rulemakings."¹⁰ This structure is useful in describing and analyzing the CDFI Jobs Portal proposal as well as assessing the costs, benefits and alternatives to its implementation. In the regulatory analysis we describe the need for the proposed rules, which primarily involves anticipated barriers that could discourage mission capital formation. We then describe the proposed CDFI Jobs Portal solution¹¹ and explain how it will meet this need. This is followed by a description of two economic baselines against which to measure the proposal's likely economic impact. In the final sections, we present a cost-benefit analysis providing an economic assessment of the proposed rulemaking, its alternatives, and the potential comparative impacts of each on efficiency, competition, and capital formation.

II. About CDFIs

⁹ Securities Act of 1933, Section 3(a)(4).

¹⁰ SEC Division of Risk, Strategy, and Financial Innovation Opportunities and the Office of the General Counsel, Memorandum: Current Guidance on Economic Analysis in SEC Rulemakings, 16 March, 2012.

¹¹ The proposal has been well received by legislators, members of the administration, securities experts, investor protection advocates, FINRA staff, CDFIs and small businesses alike.

A. What are CDFIs?

CDFIs are private financial institutions dedicated to delivering responsible, affordable lending and investment to help low-income, low-wealth, and other disadvantaged individuals and communities join the economic mainstream. By financing community enterprises—including small businesses, microenterprises, nonprofit organizations, commercial real estate, and affordable housing—CDFIs spark job growth and retention in hard-to-serve markets across the nation. CDFIs have experienced great success over the past 30 years, and have a proven track record of making an impact in those areas of America that need it most.

The CDFI Fund of the U.S. Department of the Treasury certifies financial institutions as CDFIs and administers the federal CDFI program. The CDFI Fund defines CDFIs as “specialized, community-based financial institutions that serve low-income people or work in economically distressed communities, often working in market niches that may be underserved by traditional financial institutions.”¹² Cumulatively, CDFIs have national reach, providing finance in all 50 states and the District of Columbia. There are more than 1,000 certified CDFIs operating in urban, rural, and Native communities across the United States. There are four types of CDFIs, which provide a mix of financial products to their clients: community development banks, community development credit unions, community development loan funds, and community development venture capital funds.¹³ The majority of CDFIs are also nonprofit, 501(c)(3) public charities.

B. CDFI Certification

CDFI certification is a designation conferred by Treasury’s CDFI Fund. The certification requires that qualifying financial institutions “meet the following six statutory and regulatory criteria:

- 1) Have a primary mission of promoting community development;
- 2) Serve principally an investment area or targeted population [e.g. low-income census tracts or low-income individuals];
- 3) Be an insured depository institution, or make loans or development investments as its predominant business activity;
- 4) Provide development services (such as technical assistance or counseling) in conjunction with its financing activity;
- 5) Maintain accountability to its target market; and
- 6) Be a non-governmental entity and not be controlled by any governmental entities.”¹⁴

¹² CDFI Fund. "Community Development Financial Institutions Fund United States Department of the Treasury Agency Financial Report FY 2011." CDFI Fund of the Department of the Treasury, 2012. Page 6.

¹³ Sixty-two percent of CDFIs are loan funds, 21% are credit unions, 14% are banks, and 3% are venture funds. As the CDFI Fund details: "Community development banks are for-profit corporations that provide capital to rebuild economically distressed communities throughout targeted lending and investment; Community development credit unions are nonprofit cooperatives owned by members that promote ownership of assets and savings and provide affordable credit and retail financial services to low-income people; Community development loan funds (usually nonprofits) provide financing and development services to businesses, organizations and individuals in low-income urban and rural areas and can be further categorized by the type of client served: micro-enterprise, small business, housing, and community service organizations; and Community development venture capital funds include both for-profit and nonprofit organizations that provide equity and debt-with-equity features for businesses in distressed communities." CDFI Fund. "Community Development Financial Institutions Fund United States Department of the Treasury Agency Financial Report FY 2011." CDFI Fund of the Department of the Treasury, 2012. Web. For further reference regarding the CDFI Fund program’s activities and impact, we encourage the rulemaking staff to reach out to staff of the Community Development Financial Institutions Fund of the United States Department of the Treasury, or seek any clarifications or further information from the Fund’s website at CDFIfund.gov.

¹⁴ CDFI Fund. "Community Development Financial Institutions Fund United States Department of the Treasury Agency Financial Report FY 2011." CDFI Fund of the Department of the Treasury, 2012. Page 6.

Certified CDFIs are required to have their CDFI status re-certified every three years by the CDFI Fund.

C. CDFI Activity

The CDFI sector in the U.S. collectively manages \$64.1 billion in assets¹⁵ and annually invests approximately \$6 billion in small businesses and social enterprises.¹⁶ CDFIs drive job creation as a matter of mission and purpose, and they have the capacity and expertise to focus crowdfunded capital towards the JOBS Act goal of U.S. job creation. CDFIs make loans to and invest in small business and microenterprises, residential and commercial real estate, faith-based institutions, community facilities, nonprofits, and charter schools among other social enterprises. In addition to lending activities, CDFIs often provide technical assistance and financial education programs for clients. These include assistance for small businesses as well as expanded access to savings accounts for under-banked populations.

CDFIs operate in communities throughout the United States that are not adequately served by conventional financial institutions, often due to perceptions of higher risk, higher underwriting costs and smaller average loan sizes. Utilizing the deep local-market experience of their loan officers as well as the non-standard loans in which they specialize, CDFI lenders successfully originate low-risk loans in communities that are traditionally underserved and under-banked. By investing significant resources in due diligence and technical assistance to borrowers, CDFIs balance the financing needs of their markets with the low risk tolerance of their capital sources.

The Opportunity Finance Network (OFN), the nation's largest and most prominent CDFI industry association, has tracked its member institutions' impact on communities since 1995. Through 2011, OFN reports that CDFI members have financed over \$30 billion dollars to more than 83,000 businesses and more than 9,000 unique community service organizations.¹⁷ The member CDFIs also serve clients across urban, rural, and Native areas. Forty-seven percent of CDFI clients are in major urban areas, twenty-nine percent are in rural areas, with the remainder in smaller cities and suburban areas. CDFIs also successfully serve traditionally under-banked demographic groups: minority borrowers represent fifty-two percent of CDFI clientele and forty-nine percent of CDFI clients are female.¹⁸ In addition to providing essential capital for their customers, CDFI investments often create positive, lasting impact for neighborhood or regional stabilization, economic development, health, and education.¹⁹

D. CDFIs Create Jobs

CDFIs focus on economic development in the markets they serve, including job creation, business development, and commercial real estate finance. CDFIs find and fund job-creating businesses, and in service

¹⁵ US SIF Foundation. *Report on Sustainable and Responsible Investing Trends in the United States 2012*. US SIF Foundation, Nov. 2012. Page 13.

¹⁶ See e.g., "Industry Statistics." *Opportunity Finance Network*. Page 1. <<https://www.opportunityfinance.net/industry/default.aspx?id=234>>. Industry wide data is collected by the CDFI Data Project (CDP), a CDFI industry collaborative. The CDP collected data on 495 CDFIs in FY 2008.

¹⁷ Opportunity Finance Network. "Opportunity Finance Institutions: Side by Side: Fiscal Year 2011 OFN Member Data/Analysis." Opportunity Finance Network, 2012. Page 1.

¹⁸ *Ibid.* Page 5.

¹⁹ Jacob, Katy. *Impacts of CDFIs in Illinois: A Case for an Improved Illinois Fund for Investment and Development*. Issue brief no. 21. Vol. 21. Woodstock Institute, 2003. Print. Reinvestment Alert.

of their missions, they support populations with high levels of unemployment, directing financing to disadvantaged and underinvested communities. A primary metric CDFIs use to judge their impact is job creation, which is often the greatest need in under-invested communities. A recent study of 123 CDFIs, a small subset of the 1,000 CDFIs nationally, showed that cumulatively through 2010 the studied group created or maintained nearly 500,000 jobs in many of the most vulnerable communities around the country.²⁰

E. CDFIs Are Responsible and Prudent Lenders

As local banks, credit unions, and loan funds, CDFI lenders limit risk by combining financial expertise with a deep knowledge of the local communities they serve and extensive due diligence. This has produced a long and well-established track record of responsible lending, even in communities attracting little to no investment from conventional financial institutions due to perceived higher risk. It is noteworthy that during the challenging economic climate in 2009, with 137 CDFIs reporting, the average CDFI net charge-off rate was 1.3%, while FDIC-insured institutions' annualized net charge-off rate was 2.5%.²¹ In 2010, OFN members saw a weighted average net charge off ratio of 2.0%,²² in comparison to that of all commercial banks, which was between 2.38% and 2.93%.²³ The CDFI business model involves balancing what is thought to be riskier low-income market lending with due diligence that is highly personalized to the communities CDFIs serve and strong personal relationships with borrowers.

Compared to angel investors and venture capital firms, CDFI lenders have a lower appetite for risk. CDFIs concentrate their investments in established and growth-phase enterprises with proven business models and track records, helping to ensure mission impact as well as repayment. By focusing on established business and organizations, CDFI loans are more likely to succeed than investments in startups or newer businesses, which may be the predominant investment opportunity on most crowdfunding portals.

F. Lack of Sufficient Capital Inhibits CDFI Job Creation

Lack of sufficient capital for CDFIs and their borrowers is a primary impediment to achieving even greater job creation and community impact.²⁴ As noted above, promising transactions often fail to come together due to significant financing gaps between available capital (typically a combination of CDFI financing and borrower equity) and what is needed to fully finance the transaction. The need for CDFI financing is well established and has grown in recent years. As Federal Reserve Chairman Ben S. Bernanke observed in a speech delivered at the Global Financial Literacy Summit on June 17, 2009, "even as the [financial] capacity of CDFIs has

²⁰ Jobs created: 497,277. Opportunity Finance Network. "Inside the Membership: Statistical Highlights from OFN Membership: 2010." Opportunity Finance Network, 2011. Page 1.

²¹ *Opportunity Finance Institutions: Fiscal Year 2009 OFN Member Data Analysis*. 12th ed. Page 5.

²² Fabiani, Donna. "Community Development Finance in the Southeast." *Federal Reserve Bank of Richmond*. Federal Reserve Bank of Richmond and the Opportunity Finance Network, 18 July 2012. Page 1.

²³ "Charge-Off and Delinquency Rates on Loans and Leases at Commercial Banks." *Board of Governors of the Federal Reserve System*. 16 Nov. 2012. Total of all commercial and real estate loans and leases, not seasonally adjusted.

²⁴ In supporting the Small Business Jobs Act of 2010 including the CDFI Bond Program, Senator Menendez of New Jersey stated: "As their name implies, the primary mission of community development financial institutions is to foster economic and community development in underserved areas. They have a proven track record of job creation and are arguably the most effective way to infuse capital in underserved areas for community and economic development. CDFIs leverage public and private dollars to support economic development projects, such as job training clinics and startup loans for small businesses in areas full of potential but desperate for development. CDFIs have been hit hard by the recession because they have had to rely on big banks for capital." *Small Business Lending Fund Act of 2010*. Capitol Words a Project of the Sunlight Foundation, Sept. 2010.

become more constrained, economic conditions and pullbacks by mainstream lenders have increased the demands being placed on these organizations to provide credit and services.”²⁵

CDFI’s demand for capital is driven by the growing financing needs of quality CDFI borrowers in low-income communities. The growing CDFI capital need is evidenced by increasing CDFI demand for funding from the CDFI Fund’s signature CDFI finance initiative, the Financial Assistance program. Proceeds of this program are most typically used for lending or as equity capital to leverage debt for on-lending. In FY 2011, 273 CDFIs applied for over \$454 million through the Financial Assistance program, far oversubscribing the \$139 million in available funds. Ultimately, 118 CDFIs were provided financial support.²⁶ The CDFI Fund’s New Markets Tax Credit Program, which facilitates capital investments that fill financial gaps in large-scale community development projects, shows similar demand for mission capital. The CDFI Fund noted in 2011, “since the program’s inception, 2,074 applicants have requested tax credits supporting a total of more than \$202 billion in equity investments – approximately seven times the amount of allocation available for distribution by the CDFI Fund.”²⁷

In the current climate,²⁸ borrower demand for CDFI mission capital continues to grow: in 2012, OFN members reported a significant rise in loan applications. In the fourth quarter of 2012, the most recently reported data, 64% of CDFIs reported an increase in the total number of financing applications over the previous year.²⁹ CDFIs have demonstrated a significant need for additional mission capital to respond to the growing demand for financing by responsible small businesses and social enterprises in low-income communities.³⁰

Many CDFIs report that they could make more loans if only more affordable capital were available.³¹ A thorough 2012 study noted that the cost of capital for CDFIs is “surprisingly high” given the safety and soundness of their lending programs.³² In addition to high capital costs, another significant reason CDFIs are unable to meet market demand is decreasing availability of traditional CDFI capital sources at a time of increased need.³³

²⁵ Bernanke, Ben. "Community Development Financial Institutions: Challenges and Opportunities." Federal Reserve, 17 June 2009.

²⁶ "Community Development Financial Institutions Fund United States Department of the Treasury Agency Financial Report FY 2011." CDFI Fund of the Department of the Treasury, 2012. Page 14.

²⁷ *Ibid.*, Page 22. Note that not all NMTC applicants are CDFIs, though conversations with the CDFI Fund staff suggest that CDFI demand for NMTCs is up in proportion to the stated figure.

²⁸ The capital challenge of will be further exacerbated by the effects of Sequestration, which the federal CDFI Fund has announced will cause across-the-board cuts to its CDFI-funding programs.

²⁹ "CDFI Market Conditions Fourth Quarter 2012 Report II – Detailed Tables." *Opportunity Finance Network*. Apr. 2013. Web.

³⁰ "According to The Opportunity Finance Network (OFN) 2011 2nd Quarter CDFI Market Conditions Report (a publication based on quarterly surveys of CDFIs), 54 percent of respondents reported an increase in the number of financing applications received year-over-year and 55 percent reported an increase in loan originations. Among survey respondents, 25 percent reported that they are capital-constrained and could have made more loans in the second quarter of 2011 if financing capital had been available. To meet estimated demand in the next 12 months, the respondents reported they would need an additional \$880 million in capital. Dolan, Cathy. *CDFI Bond: Opportunity of a Decade*. Rep. 2nd ed. Vol. 23. Federal Reserve Bank of San Francisco, 2011. Community Investments. Page 29.

³¹ *Ibid.*

³² The study notes that the "overall blended cost of funds for a large [CDFI] loan fund approaches 4 percent in an environment in which banks can borrow long or short-term at a much lower rate, e.g. at 0.25 percent for short-term borrowing." Swack, Michael, Jack Northrup, and Eric Hangen. *CDFI Industry Analysis Summary Report*. Publication. Durham; Carsey Institute, University of New Hampshire, NH. 2012. Page 10.

³³ A 2013 article published by the Federal Reserve Bank of San Francisco details the increased need for mission capital due to the historic decline of traditional sources of CDFI financing, including CRA and government subsidy, among other sources of financing. Bugg-Levine, Antony. "Future of

G. Crowdfunding Presents a Promising New Source of Capital for CDFIs

By deploying their extensive experience and leveraging existing CDFI resources with affordable, mission-driven, crowdfunded capital, CDFIs could meaningfully increase job creation, business investment, and other positive economic development outcomes while providing mission investors with access to safe, reliable, high-impact investments.

We are enthusiastic about the intent of the CROWDFUND Act and the potential it creates to generate new lower-cost capital³⁴ in the underserved markets CDFIs serve across the country. Access to crowdfunded capital from mission investors would allow CDFIs to responsibly channel even more capital towards job creation and economic development in these communities. By facilitating community investment, it would also allow CDFIs nationwide to leverage their extensive experience and financial knowledge while enabling community members to become stakeholders in the success of low-income communities.

III. Considerations for Rulemaking: Barriers to Mission Capital Formation

As noted above, we believe there is a risk that the rules implementing the CROWDFUND Act may inhibit mission investor participation and thus severely limit the impact CDFIs could otherwise facilitate if there were easy-to-access, broad availability of mission-based crowdfunding investments.

A. Minimum Aggregate Disclosures

A core investor protection mechanism mandated by the law is the requirement that no individual investor puts too much at risk. To that effect, the law sets out income- and net worth-based limits on what individual investors may invest annually through the crowdfunding exemption. An investor with an income or net worth below \$100,000 can invest the greater of \$2,000 or 5% of their annual income or net worth, and an investor with an income or net worth above \$100,000 can invest up to 10% of this amount.³⁵

The SEC is tasked with adopting rules for funding portals that will ensure investors do not exceed these legal limits. To do so the SEC may need to mandate that funding portals (or a data aggregating entity) verify income or net worth data to determine how much each crowdfunding investor is authorized to invest based on the appropriate percentage of his or her income or net worth. Beyond that, to ensure compliance across funding portals and participating broker dealers, the SEC may task these entities with collectively ensuring that investors do not exceed the maximum investment limits set by the law. Whether affirmed by funding portals or by some intermediary cross-sector verification service, verifying this data will require significant

Community Development: How CDFIs Can Best Ride the Impact Investing Wave" *Investing in What Works for America's Communities: Essays on People, Place & Purpose*. San Francisco: Federal Reserve Bank of San Francisco; Low Income Investment Fund, 2012. Page 150-151.

³⁴ As noted below, to eliminate "get-rich-quick" temptation by potential investors, the proposed CDFI Jobs Portal rules include limitations on rate of return for mission investors. An additional benefit of this approach is that the low cost of capital will benefit low-income community issuers to which CDFIs lend.

³⁵ Securities Act of 1933, Section 4(a)(6)(B).

(and potentially time-consuming) disclosures of personal data by crowdfunding investors. These disclosures and the time and effort they require may present barriers to entry for crowdfunding investors.

Such disclosure requirements will especially create barriers for mission investors considering small-dollar, low-return investments. The success of sites like Kiva.org (and mission- and arts-oriented offers on Kickstarter.com) demonstrates that the marketplace for mission-oriented crowdfunding is substantial. This mission-driven population will naturally be interested in charitable investing in community impact projects through securities crowdfunding. Crowdfunding mission investors are typically smaller-dollar investors seeking low or no financial return on their investment, and therefore will likely not be willing to volunteer personal identifying disclosures in order to make a small investment.³⁶ Profit maximizing investors investing more significant sums and hoping for substantial returns will be more likely to overcome these barriers to entry than will mission investors investing small sums for low return. This creates a situation wherein it will be harder to attract smaller-dollar, lower-return mission investors than profit-maximizing investors and thus funding portals serving low-return mission issuers and attracting small-dollar investors will face comparatively higher costs and time delay to attract investors for communities in the greatest need.

Highly relevant to assessing the impact of personal disclosure barriers in domestic mission crowdfunding is the experience of the international mission crowdfunding market. Kiva does not require substantial personal data disclosures, while an otherwise comparable site, MicroPlace, requires the variety of disclosures from which we propose to exempt CDFI Jobs Portals.³⁷ As detailed below, Kiva outperforms MicroPlace by approximately 11.5 to 1.³⁸ This, notwithstanding the fact that MicroPlace enjoys the backing of PayPal and offers financial return. The experience of Kiva and MicroPlace presents compelling evidence that personal disclosure requirements have a powerful stifling impact on capital formation in the context of small-dollar mission crowdfunding.

Interestingly, in the profit-maximizing context of existing peer-to-peer crowdfunding loan sites Lending Club and Prosper, crowdfunding investors are willing to overcome more substantial personal disclosure barriers.

³⁶ Requiring personal disclosures creates two distinct hurdles for investors: (1) the security and privacy concerns, and (2) the additional "friction," a term that refers to the number and nature of steps necessary to complete a transaction online, which often lead to users to "fall out" and not complete web-based transactions. Consumers regularly cite security and privacy as two primary concerns in providing personal disclosures online. Small-dollar investors with lower financial incentives are less likely to overcome these barriers, and are more likely to exit during the steps to completing a transaction. There is a rich body of research studying consumer behavior response to private information requests online in two relevant sectors: online banking and e-commerce. In online banking, a 2006 survey conducted by Michigan Surveys of Consumers and published by the Federal Reserve found just 40% of users "feel comfortable providing personal information through electronic banking systems," (Bell, C. J., Hogarth, J. M., & Robbins, E. (2009). U.S. Households' Access to and Use of Electronic Banking, 1989-2007. *Federal Reserve Bulletin*, A99-A121.), and in e-commerce surveys on consumer disclosure, users' Social Security Numbers were considered to be the most private piece of information and most regularly falsified (Metzger, M. J. (2004), Privacy, Trust, and Disclosure: Exploring Barriers to Electronic Commerce. *Journal of Computer-Mediated Communication*). In addition, a study conducted by Dan Zarella of Hubspot examined the correlation between a user completion of a desired action, and the number of text boxes, and found the increase of 'steps' leads to a decrease in the total completions of the action (*Which Types of Form Fields Lower Landing Page Conversions?* 11 Oct. 2010. Web.). Even for users not dissuaded by the notion of personal disclosure, any required documentation would be time consuming to locate and upload and thus likely to decrease participation, which will be true for first time users regardless of whether such disclosures are made on CDFI Jobs Portal or on a data sharing regime as some have recommended. Disclosure documentation would be time consuming to locate and upload, and these steps would decrease participation.

³⁷ As noted in Section V.B.3.(c), page 31 below, before investing through MicroPlace, users must disclose his/her social security number, and self-verify income, liquid net worth, income tax bracket, and investment knowledge and experience. A Kiva investor, by contrast, simply enters his/her credit card number as well as physical and email address, which are customary internet disclosures.

³⁸ See below in Section V.B.3.(c), page 31.

Both platforms require disclosure of Social Security Number and other personal data. They attract larger average investment sizes than mission crowdfunding while offering much higher rates of return³⁹ In comparison, Kiva loans offer 0% return while MicroPlace offers investments of between 0.5% and 4% with an estimated average of 1%⁴⁰. This suggests that the challenge of overcoming disclosure barriers may be more severe for small-dollar, lower-return crowdfunding offerings, such as those proposed for CDFI Jobs Portals. Based on this evidence, personal barriers may be less likely to compromise capital formation by profit-maximizing funding portals.

B. Limits on Marketing

The CROWDFUND Act prohibits funding portals and issuers from advertising the terms of a crowd-funded offering. Without a clarification in the rules that permits advertising of non-financial, mission elements of a transaction this prohibition in the Act will likely present a significant barrier for mission issuers and investors.

U.S. crowdfunding campaigns to date have not promised financial returns but have been successful because of viral marketing efforts launched by portals and issuers.⁴¹ Most Title III offerings will hold the prospect of substantial financial return for investors and this investor profit motive may lessen the marketing need for most securities crowdfunding. This will not be the case for mission issuances. These issuances will offer only minimal financial return and will attract investors based on charitable motivations. Similar to non-securities crowdfunding, mission-focused investors will be most successfully made aware of community development crowdfunding offerings through advertising and viral marketing kicked off by the issuer or portals. Preventing any type of messaging outside of a simple notice would seriously compromise the ability to reach mission investors.

We believe a clarification by the SEC permitting advertising of non-financial, mission elements of a transaction⁴² is appropriate in the case of CDFI Jobs Portals, which are driven exclusively by mission impact and provide substantial, supplementary investor protections.

In summary, the large and growing marketplace of mission investors could drive capital formation resulting in tremendous job-creating impact. But there is a risk that implementation of the investor protection regime – which may include personal data disclosure requirements and marketing limitations – may prevent or severely limit mission investor participation unless the rules are developed with the unique attributes of mission investors in mind.

³⁹ Lending Club's two-week average interest rate for all loan terms is 15.26%, and an average interest rate of between 7.61% (for the "A" Lending Club Credit Rate) and 23.61% (for the "G" Lending Club Credit Rate). Source: *Lending Club Statistics*, accessed 25 July 2013. <<https://www.lendingclub.com/info/statistics-performance.action>>. Prosper's average rate of "seasoned returns" of 9.28%, and an average interest rate of between 5.5% (for the "AA" Prosper Credit Rate) and 13.29% (for the "HR" Prosper Credit Rate). Source: *Prosper Marketplace Performance* accessed 25 July 2013.

⁴⁰ Source: Klein Bier, Jerilyn. "Low-Cost Impact Investing." *Financial Advisor Magazine*. 28 Sept. 2012. Web. <<http://www.fa-mag.com/news/low-cost-impact-investing-12104.html>>, and "Kiva - About Us." *Kiva - Stats*. Data from up to 8 June 2013. <<http://www.kiva.org/about/stats>>. Note: MicroPlace average return estimates are based on 28 the offerings that were active as of 26 June 2013.

⁴¹ See, e.g. "Crowdfunding Is Marketing Pure and Simple." *Small Business Marketing Blog from Duct Tape Marketing*. 29 Aug. 2012; and "How to Make Your Crowdfunding Go Viral? Growthink Reveals the 4 Keys to Crowdfunding Success." 1 June 2012.

⁴² See Appendix A, Rule XX01(a)(iii).

IV. CDFI Jobs Portals: Strengthening Investor Protections While Reducing Barriers to Participation

We support a solution that would introduce a supplementary set of strong investor protections while reducing the above-described barriers for mission investors. The core concepts of this solution were first introduced in a Statement for the Record on July 26, 2012 by Senator Jeff Merkley,⁴³ co-author of the CROWDFUND Act. The proposed rules are designed to protect investors, facilitate mission capital formation, and create an orderly, transparent marketplace for small-dollar mission investors. As Senator Merkley stated:

“Because of the types of businesses CDFIs work with, the types of low returns that might be derived, and the particular financing gaps that might be filled through crowdfunding...mission-driven, CDFI-supported crowdfunding may yield better results for investors and positive job creation for communities if the rules reflect the particular work they do. Suggestions include ensuring crowdfunding can fill the financing gap for projects supported by federally-regulated, 501(c)(3) CDFIs, a clarification to ensure that CDFIs and issuers can make sure investors understand the mission and charitable aspects of investments.”⁴⁴

A. Proposed Permissions to Enhance Mission Capital Formation

In light of the substantial investor protections detailed in the next section, we believe it appropriate for the SEC to adopt accommodations that support mission capital formation through CDFIs as introduced by Senator Merkley. These permissions would include reducing the anticipated personal disclosure requirements for investors who invest less than \$500 and clarifying marketing standards surrounding mission impact,⁴⁵ as items are detailed below.

1. Reducing Personal Data Disclosures for Cumulative Investments Under \$500

Since a requirement for personal data disclosure would inhibit small dollar, low-return mission investors,⁴⁶ we support an exemption from data disclosure for investors who invest less than \$500 on CDFI Jobs Portals, in aggregate, per year on CDFI Jobs Portals (or, in the alternative, a low-threshold “check-the-box” verification solution). We recommend CDFI Jobs Portals require personal disclosures once an investor crosses the \$500 total investment threshold across CDFI Jobs Portals.⁴⁷

Senator Merkley, in his statement for the record, recommended the SEC consider “ordinary investors that remain within...\$500 on any one platform [be] presumed compliant across other unaffiliated platforms. This streamlining may be particularly useful for those seeking to...engage in community-based crowdfunding, including those serving the CDFI community.”⁴⁸ We are not sure the SEC will conclude that the presumption of compliance is consistent with the mandate in the law to enforce the investor limits. (For instance, it has been suggested that an investor could invest \$500 on dozens or hundreds of funding portals, thereby far

⁴³ Senator Jeff Merkley (OR). "Crowdfunding." *Congressional Record* 158:113 (July 26, 2012) page S5474.

⁴⁴ *Ibid.*, Pages S5477- S5478.

⁴⁵ Senator Jeff Merkley (OR). "Crowdfunding." *Congressional Record* 158:113 (July 26, 2012) page S5474.

⁴⁶ See above Section III. A., page 10.

⁴⁷ See Appendix A, Rule XX(a)(ii)(A)(I) and (a)(ii)(A)(II).

⁴⁸ Senator Jeff Merkley (OR). "Crowdfunding." *Congressional Record* 158:113 (July 26, 2012) page S5474.

exceeding the law's investment limits.) We therefore recommend investors who remain within \$500 in aggregate investment across all CDFI Jobs Portals be "presumed compliant." – or effectively be subject to lower personal disclosure requirements of name and address. The collection and tracking of names and addresses would likely be the primary way in which CDFI Jobs Portals complied with the proposed aggregate \$500 limit. The number of federally regulated 501(c)(3) CDFIs is small and so the number of CDFI Jobs Portals will be small. For this reason, CDFI Jobs Portals will be able to communicate with one another easily to reasonably ensure that investors do not exceed limits by sharing available identifying data (names and addresses), consistent with Gramm-Leach-Bliley privacy rules.⁴⁹

While this standard may be easier to circumvent than a higher standard of personal disclosure would be, it is reasonable given the protections CDFI Jobs Portals provide. Because CDFI Jobs Portal offerings only offer low rates of return, little incentive will exist for investors to make the effort to undermine the rules in order to invest more. Furthermore, given the highly regulated, mission focus of CDFI Jobs Portals, the SEC can be confident investors will not be subject to coercive or fraudulent tactics to push investors beyond their investment limits through "pump and dump" or other schemes.

This is not a recommendation that the SEC allow across-the-board exemptions from the personal disclosure requirements for small-dollar investments. Low-income investors, who can least afford financial loss, will disproportionately provide small dollar investments and we are aware of the SEC's findings that low-income and minority communities are often targets of investor abuses and scams.⁵⁰ Some have pointed out that crowdfunding loss and fraud may be more likely in the small dollar crowdfunding space, where enforcement will be harder to pursue.⁵¹ For these reasons, we recommend the personal disclosure requirements be consistent across investment amounts unless strong alternative protections such as those proposed herein are provided.

2. Permit Advertising for Mission Aspects of Offerings

For CDFI Jobs Portals offering the suite of protections outlined below, we recommend that the SEC clarify the rules that regulate the advertising of offerings by issuers and portals.⁵² The CROWDFUND Act prohibits advertising the terms of offerings. We recommend allowing CDFI Jobs Portals and issuers to market the projected non-financial, mission-impact elements of posted offerings.

Marketing of projected charitable impact will facilitate mission capital formation and is consistent with the law's intended investor protection prohibiting the promotion of investment terms which presumably include transaction elements such as rates of return, maturities and ownership stakes. We do not believe mission elements of the transaction constitute "terms of the offering" per Securities Act of 1933, §4A(b)(1)(H)(2).

⁴⁹ To ensure that investors are not able to exceed their overall investment limits (for instance that an investor earning \$50,000/year and able to invest \$2,500 based does not invest \$3,000 and thereby exceed their legal maximum investment), CDFI Jobs Portals should be permitted to interface with any platform the broader crowdfunding sector uses, identifying users via name and address. CDFI Jobs Portals will also enable those investors who have already complied with the higher disclosure requirements of conventional portals to participate through the existing sector-wide platform.

⁵⁰ "Affinity Fraud: How To Avoid Investment Scams That Target Groups." Securities and Exchange Commission. *Investor Alert: Affinity Fraud*. Web.

⁵¹ See e.g. Johnson, Antone. "The Great Crowdfunding Train Wreck of 2013." Web. *Gust*. 19 Mar. 2012. Web.

⁵² See Appendix A, DEFINITIONS, (b)(ii)

Such items may include charitable elements such as jobs created, populations served, green impact, children educated, and other intended non-financial mission outcomes. Providing this clarification on advertising limitations as part of the proposal is appropriate given that CDFI Jobs Portals provide numerous more stringent investor protections than would other portals.

B. Proposed Investor Protections: Stronger Protections That Will Not Inhibit Mission Investor Participation

The proposed solution involves introducing strong investor protections administered by a specific type of crowdfunding portal, referred to as a CDFI Jobs Portal, through which mission investors can co-invest in CDFI-funded projects and businesses. Crowdfunded debt securities co-invested alongside CDFIs through CDFI Jobs Portals will typically fill financing gaps, which, as noted above, frequently prevent CDFI transactions from coming together.⁵³

1. CDFI Jobs Portal: Investor Protections Overview

In seeking to reduce the anticipated barriers to mission investors that may come as a result of certain investor protections, a central objective of the proposed rules is to supplement the relaxation of these protections (detailed in the previous section IV, A) with a series of alternative investor protections that are more stringent than those required by law but that do not present barriers for mission capital formation. The table below outlines the investor protections extended through the CDFI Jobs Portal and compares them to the anticipated rules for standard portals.

| <i>Investor Protections</i> | Jobs Portal | Standard Portal |
|--|--------------------------------------|------------------------|
| Sophisticated co-investor “skin in the game” | Yes | No |
| Strict standards & ongoing quality control of co-investors | Yes | No |
| Issuer “skin in the game” | Yes | No |
| Restricted to lower-risk loans with low rates of return | Yes | No |
| Proven financial strength overseen by Federal regulators | Yes | No |
| Subject to Gramm-Leach-Bliley privacy rules ensuring investor privacy protection | Yes | No ⁵⁴ |
| Investor personal data disclosure for tracking maximum aggregate investment | Over \$500: Yes \$500 or less: No | Yes |

C. The CDFI Jobs Portal: Investor Protections Detail

As summarized above, the CDFI Jobs Portal solution contains a number of supplementary investor protections that go beyond those required in the law. This section details each.

⁵³ Using CDFI Jobs Portals, crowdfunding investors could also potentially lend directly to CDFIs, so long as the CDFI-issuer itself has been invested (and underwritten by) a separate qualified CDFI. In this case, crowdfunded capital would most typically be on-lent to the CDFI-issuer’s low-income community borrowers.

⁵⁴ While participating broker dealers will be subject to Gramm-Leach-Bliley rules (GLB), and while the SEC may find GLB a valuable standard for enforcing Title III’s privacy protection mandate, it is not clear that any approximation of this pre-established and separately enforced standard could be applied effectively to otherwise unregulated funding portals.

1. CDFI Co-Investor “Skin in the Game” Requirement

Every transaction posted on a CDFI Jobs Portal must have a co-investment (“skin in the game”) from a CDFI.⁵⁵ The co-investment structure, which was also proposed in the report resulting from the Milken Institute’s 2012 crowdfunding roundtable, “would allow the crowdfunded businesses and crowdfunding investors to benefit from the due diligence and management expertise of sophisticated investors,” helping ensure legitimacy of issuers and the soundness of investment.⁵⁶

The SEC has also cited the participation of a sophisticated financial intermediary as a source of protection against fraud. Most recently, this compelling reasoning appeared in the text introducing the proposed rule that would eliminate the ban on general solicitation in offerings under Rule 506 of Regulations D and in Rule 144A offerings. In suggesting that instances of fraud would be less likely in the case of generally solicited 144A offerings, the proposing release noted:

“We expect that there would be fewer occurrences of general solicitation facilitated fraud in Rule 144A offerings, as compared to Rule 506(c) transactions.... Rule 144A offerings always include a financial intermediary. The due diligence conducted by these intermediaries is an additional layer of protection against fraud.”^{57, 58}

2. CDFI Co-Investor Performance Standards Requirement

As a further measure to ensure investment soundness, the co-investing CDFIs themselves would be required to meet high performance standards (loan loss rates, reserves, capitalization). These standards would be established and enforced by the CDFI Jobs Portal, ensuring that only financially strong CDFI co-investors are able to participate.⁵⁹ In a sector with very low loss rates, participation would be limited such that any poor loan performance outliers or the rare at-risk institution would be excluded.

CDFI sector expertise, combined with these co-investor quality control standards, provides substantial assurance that issuers will not be fraudulent enterprises. Beyond simply weeding out fraud, the standards will also contribute to the likelihood that issuances are of good quality, with a very high likelihood of

⁵⁵ See Appendix A, Rule XX01 (b)(ii)(C). Note that the qualified CDFI co-investment is not in the same crowdfunded security, but does support the same transaction. This co-investment may be a bank loan or credit facility or securities that are offered in a registered offering or pursuant to an exemption from registration such as Section 4(a)(2) or Regulation D.

⁵⁶ Gorfine, Daniel S., Bradley Belt, and Chris Brummer. “Crowdfunding: Promoting the Promise and Minimizing the Peril.” *Milken Institute*, Aug. 2012. Web. Page 6. See also Gorfine, Daniel S., and Chris Brummer. “Crowdfunding: The Next Big Thing” *The Milken Institute Review*. First Quarter, 2013. Which urges the SEC to “consider a ‘green-light’ model that reduces the regulatory burden on portal-based transactions that couple the crowd with accredited investors” including CDFIs. Page 71.

⁵⁷ In this report, the SEC staff further states: “Also, Rule 144A investors are generally large institutions, which are better able to identify fraudulent activities than smaller institutions and retail investors.” “SECURITIES AND EXCHANGE COMMISSION 17 CFR PARTS 230 and 239 [Release No. 33-9354; File No. S7-07-12] RIN 3235-AL34 ELIMINATING THE PROHIBITION AGAINST GENERAL SOLICITATION AND GENERAL ADVERTISING IN RULE 506 AND RULE 144A OFFERINGS.” Securities and Exchange Commission, 27 Aug. 2012. Web. Page 53.

⁵⁸ While many CDFIs are smaller institutions, it is broadly recognized in the banking sector that in the case of community development finance, these smaller, community-based financial intermediaries better perform the thorough due diligence necessary for investment success because of their deep knowledge of local markets and market players and close ties to the community. Recognition of this expertise is a primary reason that the banking industry is the largest investor in the CDFI sector, providing roughly 40% of the sector’s capital. Larger banks find that CDFIs can more effectively and reliably provide this type of smaller scale, less-systematized finance than can larger institutions.

⁵⁹ See Appendix A, Rule XX01 (b)(i)(A)&(B).

repayment, as they will have been competently reviewed by stable CDFI co-investors with strong track records.

3. Requirement of Issuer First-Loss Co-Investment

In addition to the requirement of a qualifying CDFI co-investor, each issuer must also invest or put at risk its own resources in order to be eligible for a crowdfunding investment through a CDFI Jobs Portal. This issuer “skin-in-the-game” will be equity or equity-equivalent resources that serve as “first-loss” funds in the event of default.⁶⁰ The CDFI Jobs Portal will be responsible for affirming (with the assistance of the CDFI co-investor) that issuer resources have been committed before an offering can post on the site.

4. Low-Return Debt: Emphasizing Charitable Nature of Investment, Removing Enticement of High Returns

Securities offered on the CDFI Jobs Portal will be restricted to low-yield debt investments, attracting investors who are motivated more by the mission impact of the offering than by its potential financial return. Before investing, each investor will also be required to affirm a simple, easy-to-read statement acknowledging that they are making a mission investment that offers below-market rates of return and that all funds are at risk of loss.⁶¹ The rate-of-return limitation,⁶² restriction to debt, and acknowledgement of mission investment help make clear the non-profit-maximizing, charitable nature of the investment. Further, to the extent the “get-rich-quick” temptation is one aspect of securities investing that leads investors to take on greater risk than perhaps they can afford, these mechanisms are intended as a form of investor protection dissuading investors from any inclination to take on significant exposure through CDFI Jobs Portals for the sake of financial return.

The limitation of these offerings to debt securities will likely be attractive to issuers on CDFI Jobs Portals. Small businesses in low-income communities, most of which have never offered equity securities before, would likely not find appealing the ongoing costs of offering equity. In particular, it has also been noted that the complexities and costs of ongoing services and reporting to large numbers of equity investors as well as related compliance costs will be difficult to manage and/or generally unappealing for small businesses unaccustomed to this work.⁶³

5. Regulated Financial Institution Requirement

Senator Merkley’s Statement for the Record references federally regulated, 501(c)(3) CDFIs.⁶⁴ The proposed rule requires that CDFI Jobs Portals be controlled or operated by such entities: regulated financial institutions that are also both public charities and certified CDFIs. The requirement that the entity be controlled or operated by a federal banking agency will help ensure investor privacy protection as well as successful

⁶⁰ See Appendix A, Rule XX01 (b)(i)(C).

⁶¹ This statement, in addition to the requirement as prescribed in Title III that each investor “positively affirms that the investor understands that the investor is risking the loss of the entire investment, and that the investor could bear such a loss” as reflected in Securities Act of 1933, Section 4A(a)(4)(B).

⁶² We propose that the maximum annual rate of return of 5%.

⁶³ Graham, Stephen M. "The JOBS Act Represents An Important Step in the Right Direction." Fenwick & West LLP, 2012. Web. Graham notes that “the administrative costs involved in managing hundreds of shareholders could be significant.” Page 1. In addition, nonprofit organizations, which constitute a large portion of CDFI borrowers, are non-stock corporations that are unable to offer equity to investors.

⁶⁴ Senator Jeff Merkley (OR). "Crowdfunding." *Congressional Record* 158:113 (26 July 2012) page S5474.

execution of the investor protections summarized above. Relevant federal financial institution regulators include the Office of the Comptroller of the Currency, the Federal Reserve Board, and the Federal Deposit Insurance Corporation. These regulators, also known as “federal banking agencies” regulate national banks, state-chartered banks, bank holding companies, and credit unions. These regulators also oversee any 501(c)(3) CDFI affiliates their regulated financial institutions may control.

The requirement of an additional regulator beyond the SEC is not to regulate CDFI Jobs Portals for securities law compliance, as this is the role of the SEC (and FINRA). Rather, it is intended as an additional and important layer of oversight to ensure the stability and responsibility of CDFI Jobs Portals and the institutions that operate them. These regulators regularly and thoroughly review financial institutions for financial strength and stability as well as reputational risk, *inter alia*. This additional non-securities regulatory oversight ensures that operators of CDFI Jobs Portals are well-established and responsible financial enterprises.

These regulators ensure strong and responsible financial management and will manage CDFI Jobs Portals with high standards of quality control. They will likely focus on ensuring that CDFI Jobs Portals work with responsible issuers and co-investing CDFIs. Furthermore, since status as a regulated financial institution is difficult to attain, it ensures ‘fly-by-night,’⁶⁵ and high-risk enterprises will not be able to operate CDFI Jobs Portals. From the SEC’s regulatory cost perspective, this provision also effectively restricts the number of entities that can operate a CDFI Jobs Portal, limiting the number of portals subject to this special SEC rule while opening the market up to broad participation in the CDFI sector through CDFI co-investing.

There is also strong precedent for the SEC providing exemptive relief to regulated financial institutions in the distinct but related context of securities issued by these entities. Section 3(a)(5)(A) of the Securities Act of 1933 exempts from regulation “any security issued (A) by a savings and loan association...cooperative bank...or similar institution, which is supervised and examined by State or Federal authority having supervision over any such association.” While these financial institutions are not issuers when operating CDFI Jobs Portals, we believe that the long-standing precedent in federal securities law recognizing the unique role and supplementary supervision of regulated financial institutions as supportive justification for exemptive relief from securities regulation is relevant in this context.

The requirement that CDFI Jobs Portals be subject to regulation by federal banking agencies also helps to ensure strong privacy protection for its investors. Federally regulated financial institutions are governed by Gramm-Leach-Bliley privacy rules, and these privacy protection rules would also apply to any funding portal they control. As a result of this fact, CDFI Jobs Portals will be legally bound to protect the confidentiality of customer data and additional federal banking regulator oversight will ensure that they do so. The

⁶⁵ In early conversations in which we suggested all CDFIs be able to operate “low-barrier to entry” crowdfunding portals, it was pointed out in conversations with policy makers that a bad actor could theoretically operate as a legitimate mission lender for several months in order to attain CDFI status, with a long-term intent to defraud investors. While this would be conceivable for the attainment of CDFI certification, the standard for becoming a federally regulated financial institution is much higher. Such a scheme would not be possible in the context of the proposed financial institution requirement for operating CDFI Jobs Portals. Furthermore, because CDFI Jobs Portals would have higher standards for participating CDFI co-investors than the standard for becoming a CDFI (see item 2 in this Section), the portals would effectively weed-out any potential bad actors.

CROWDFUND Act's requirement that the SEC develop and enforce privacy requirements for funding portals⁶⁶ should be comfortably met by this standard.

6. Public Charity Requirement

The proposed rules require that CDFI Job Portals be operated or controlled by public charities.⁶⁷ As 501(c)(3) public charities, operators of CDFI Jobs Portals will be legally bound to pursue charitable purposes, providing an additional layer of assurance of charitable activity as well as accountability to the IRS for achieving charitable purpose. Federal securities law and the SEC have an established history of accommodating securities regimes that responsibly achieve charitable purpose goals.⁶⁸ While a CDFI Jobs Portal would not be the issuer itself, in purpose and design the proposal is consistent with Congress's exemptive intent for charitable purposes.

In addition, a substantial portion of co-investors and issuers of these crowdfunded securities will be public charities as well. While not all issuers would be public charities, all will have positive community impact either directly through their work or indirectly through their community impact, as all will have been co-funded by federally accredited CDFI mission investors and approved for posting based on their charitable impact by the public charity CDFI Jobs Portal.

It is important to note that neither the Securities Act of 1933 nor the Philanthropy Protection Act of 1995 provides any exemption for public charities from the anti-fraud provisions.⁶⁹ The CDFI Jobs Portal will be subject to the same anti-fraud provisions.

As referenced above, federal securities law and the SEC have long supported the exemption of charities from many aspects of securities regulation. Since its inception, the SEC has provided broad exemptions for public charities and benevolent organizations because they serve the public interest. The intent of these exemptions is both to make it easier for the broader public to invest for the public good and also to make it less costly for entities serving the public good – which typically lack the resources to engage in the securities registration process – to access capital. The proposed CDFI Jobs Portal rules are designed to apply this well-established exemptive charitable precedent to the crowdfunding rulemaking now before the Commission.

D. Reducing Barriers to Enhance Mission Capital Formation

As we submit these general comments, we of course do not know what the proposed crowdfunding rules will be. Our comments thus address anticipated potential barriers for mission investment. Above, we suggest implementing rules that will encourage mission investor participation – rules that allow fewer personal disclosures and marketing of mission impact – when supplemented by CDFI Jobs Portal investor protections.

⁶⁶ Securities Act of 1933, Section 4A(a)(9).

⁶⁷ See Appendix A, DEFINITIONS, (b)(ii).

⁶⁸ Section 3(a)(4) of the Securities Act of 1933 outlines the exemption from registration for "[a]ny security issued by a person organized and operated exclusively for religious, education, benevolent, fraternal, charitable, or reformatory purposes and not for the pecuniary profit, and no part of the net earnings of which inures to the benefit of any person, private stockholder, or individual."

⁶⁹ For further details on public charities and securities regulation, we encourage the rulemaking staff to read "Securities Regulation of Fundraising Activities of Religious and Other Nonprofit Organizations." Horner, Timothy L. and Makens, Hugh H., *Stetson Law Review*, (1996).

We also urge the Commission, in promulgating its rules for crowdfunding participants (funding portals, issuers, and investors), to consider additional factors to enhance mission capital formation.

We encourage the SEC to consider the extent to which any rules may increase the costs of funding portal operations, increase the complexity or costs for issuers, or create potential unnecessary barriers or inconvenience for charitable mission investors (as such may be identified in the SEC's own cost-benefit analysis of its rules). We ask that the SEC further consider providing exemptions from any potentially cost-inducing rules for those participants that are operating under the more stringent CDFI Jobs Portal regime. Such relief may be justified where the cost-inducing rules are intended to remedy problems that the CDFI Jobs Portal regime solves independently.

The CDFI Jobs Portal concept is designed to create an efficient, transparent, low-cost marketplace relying on CDFI systems and structures that already exist and function well. Because CDFI Jobs Portals go beyond the requirements of the law to impose a series of meaningful investor protections, we believe it is also appropriate for the SEC consider making it simpler for CDFI Jobs Portals to achieve their mission capital formation objectives, by:

- allowing user search based on various factors,⁷⁰
- permitting CDFI Jobs Portals to accept payment by credit card, and
- enabling call rights for issuers and CDFI co-investors.⁷¹

Beyond the consideration that exemptions and permissions may be justified based on the strong alternative investor protection provisions to which CDFI Jobs Portals and their participants would subject themselves, exemptive relief from any cost-inducing rules is also justified because doing so is in the public good and serves the public interest.

E. Support for Safe Harbors when Paired with Strong Investor Protection

Both Title III co-author Merkley and the Milken Institute have encouraged the SEC to consider creating exemptive "safe harbors" within the regulations for funding portals operating with mechanisms that prioritize investor protection or reduce the risk of fraud for investors. The Milken Institute recommends the consideration of "safe harbors for particular types of ventures, including those focused on community development or social philanthropy,"⁷² and in two publications the Milken Institute specifically names CDFIs as appropriate co-investors. Senator Merkley likewise suggests that the SEC "might even adopt safe harbors for simple, investor-friendly structures"⁷³ and, as noted above, identifies CDFIs as a promising vehicle. Both sources recommend that where strong systems are in place to protect investors, the SEC should consider

⁷⁰ Including cause, geography, offering opening date and time remaining, percentage funded, impact metrics, and key words.

⁷¹ This would effectively permit pre-payment of crowdfunded notes without penalty or acceleration of interest due.

⁷² Gorfine, Daniel S., Bradley Belt, and Chris Brummer. "Crowdfunding: Promoting the Promise and Minimizing the Peril." *Milken Institute*. Aug. 2012. Web. Page 10., and Gorfine, Daniel S., and Chris Brummer. "Crowdfunding: The Next Big Thing" *The Milken Institute Review*. First Quarter, 2013. Which urges the SEC to "consider a 'green-light' model that reduces the regulatory burden on portal-based transactions that couple the crowd with accredited investors" including CDFIs. Page 71.

⁷³ Senator Jeff Merkley (OR). "Crowdfunding." *Congressional Record* 158:113 (July 26, 2012) page S5474.

how to provide safe harbors from potential barriers to participation in order to facilitate greater capital formation. The CDFI Jobs Portal solution is consistent with these recommendations.⁷⁴

V. Cost-Benefit Analysis

A. The Baseline Against Which to Measure The Proposal's Economic Impact

In this section we seek to describe the economic baseline for the proposed rulemaking and also the state of efficiency, competition and capital formation in the absence of the proposed CDFI crowdfunding rules for mission investors. Two relevant baseline situations inform the proposed rulemaking and its likely impact. These include:

1. *The baseline status of access to capital for CDFIs and their low-income community borrowers*
2. *The baseline in the currently active crowdfunding marketplace*

1. Measuring the Baseline: Access to Capital for CDFIs and Their Low-Income Community Borrowers

(a) An Inefficient Marketplace for an Important Capital Source: Individual Mission Investors

As noted above,⁷⁵ lack of sufficient capital for CDFIs and their borrowers substantially impedes greater job creation and low-income community impact. Critically important to our baseline consideration of CDFI and low-income community access to capital is that a significant source of mission capital is largely not accessed by the CDFI sector: individual investors.

The CDFI sector primarily depends on institutional capital including equity and debt from financial institutions, government sources, and private philanthropies, which historically have provided 80-90% of the sector's total capital.⁷⁶ Individuals, on the other hand, have provided a small portion of the sector's capital, historically 10-20%.⁷⁷ There is a marked contrast between charitable investing and charitable giving. In the donations space, individual donors provide over 80% of philanthropic giving while institutions (corporations, foundations, etc.) provide less than 20% of all donations.⁷⁸ This striking disparity between the newer field of charitable investing and the long-established field of charitable giving suggests a market inefficiency in the charitable investing space.

⁷⁴ Beyond enhancing mission-driven capital formation, it is our hope that our proposal to pair additional protections with somewhat greater latitude provides useful experience that might advance the long-run growth of crowdfunding generally. The experience and ultimate effectiveness of a "sophisticated co-investor" approach (along with other controls) provides a low-risk way for the SEC to broaden access to crowdfunding while potentially helping to inform the SEC's future rulemaking in this area.

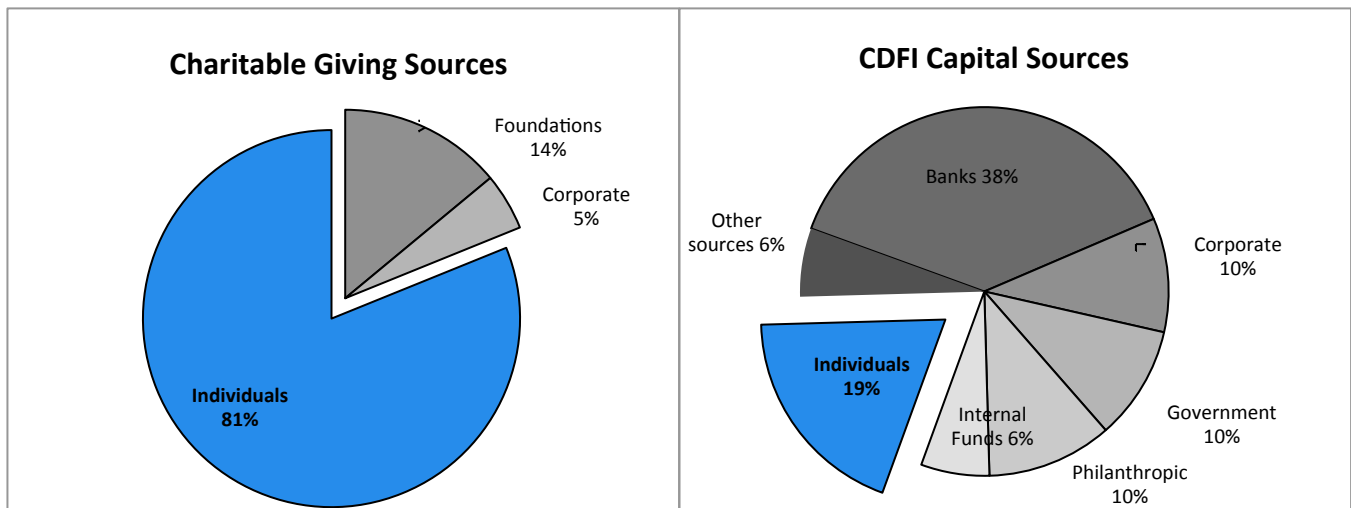
⁷⁵ See above in Section II.F., page 8.

⁷⁶ In this context, "capital" encompasses both debt and equity for CDFIs. *The Financial Crisis and CDFIs: A Brief Look at 2007-2009 CIIS Data*. Presentation. Financial Strategies & Research Community Development Financial Institutions Fund, 2010. Print. Page 6.

⁷⁷ *Ibid.*, Page 6.

⁷⁸ Giving USA 2011: The Annual Report on Philanthropy, a publication of Giving USA Foundation™, researched and written by the Center on Philanthropy at Indiana University.

Sources of Mission Funding ⁷⁹



Individuals seeking to make charitable donations enjoy many settled methods and paths to achieve their objectives. In contrast, there are not currently simple ways for individuals to engage in charitable investing or for CDFIs to access individual investors. CDFIs currently must access mission investors through the costly federal and/or state securities processes. Since most CDFIs are nonprofits, exempt from federal securities laws, this primarily involves securing multiple state-level exemptions. However, even this least-costly option often costs over \$200,000 including significant legal fees, plus administrative costs and marketing costs. These substantial expenses and other hurdles render small capital raises impractical and larger capital raises time consuming and challenging. The status quo does not represent a cost effective, orderly, or efficient marketplace for capital formation.

From the individual perspective, the document-heavy process of mission investing is time consuming and can be intimidating. From the CDFI perspective, there is real cost to successfully attracting each individual investor, rendering it cost prohibitive to raise funds from the “long tail” large population of smaller-dollar investors whose aggregated capital could be meaningful to low-income communities.⁸⁰ This inefficient and costly process means that an otherwise plentiful potential source of capital remains almost entirely untapped by CDFIs. Crowdfunding, if implemented in a way that works for mission investors and CDFIs, presents a new and powerful opportunity to channel individual investor capital to under-invested communities.

(b) The Effects of Insufficient CDFI Capital Supply on Low-Income Communities

⁷⁹ The chart "Charitable Giving Sources" is derived from the report Giving USA 2011: The Annual Report on Philanthropy, a publication of Giving USA Foundation™, researched and written by the Center on Philanthropy at Indiana University. The chart "CDFI Capital Sources" is derived from an average of *The Financial Crisis and CDFIs: A Brief Look at 2007-2009 CDFIs Data*. Presentation. Financial Strategies & Research Community Development Financial Institutions Fund, 2010. Print. Page 6.

⁸⁰ CDFI banks and credit unions can also raise individual investor capital through deposits, but achieving status as a federally regulated depository is costly and time consuming and does not fit the business model of most CDFIs. Moreover, many parts of the country are served only by non-depository CDFIs.

Demand for CDFI capital significantly outstrips supply. A 2011 study of a subset of 136 CDFIs (out of a total of over 1,000 nation-wide) noted that these CDFIs faced a capital demand shortfall of \$880 million over a 12-month period;⁸¹ for the entire CDFI sector this gap is almost certainly much larger. The insufficient supply of mission capital produces three primary outcomes in low-income community finance.

The first and most obvious outcome of this inability to meet borrower demand is that many good, job-creating community transactions simply don't come together. Community enterprises that are fundable often cannot fill their total capital need due to CDFI lender limitations (and/or lack of viable subordinate finance or subsidy), resulting in financing gaps that prevent transactions from closing. While not every transaction is viable, a tremendous number of projects would be viable if a greater amount of mission capital were available to fund them or to fill these financing gaps.

A second outcome is that the lack of access to mission capital forces CDFIs and their borrowers to use alternative, higher cost capital in ways that can compromise community impact. For instance, despite investment performance similar to that of conventional banks, CDFIs can face short-term debt costs as much as 16 times the rate paid by banks.⁸² In some cases transactions are successfully brought together, but with higher cost capital than is ideal for a low-income community project. This happens in one of two ways: CDFIs raise higher-cost funds (once lower-cost sources are exhausted), the cost of which must be passed on to borrowers at higher rates; or, in the alternative, borrowers themselves take on even higher-cost, third-party mezzanine financing. In either case, the community enterprises that can afford this higher-cost capital must do so at the expense of programmatic impact.

The third outcome of insufficient CDFI access to mission capital is that in order to ensure community transactions come together and/or to avoid mission-compromising higher-cost capital, CDFIs and their borrowers dedicate a tremendous amount of time and effort to fill financing gaps by seeking subsidy or low-cost capital from other CDFIs, philanthropies, and government sources. In such cases transactions do come together, but at a much higher capital-sourcing cost than if a significant source of gap-filling capital were readily available, such as through an efficient, dedicated crowdfunding platform.

(c) Addressing Market Inefficiencies through CDFI Jobs Portals

In summary, the CDFI sector is achieving significant job creation and other charitable impact but at the same time has the capacity to achieve more impact if the sector and its borrowers had greater access to lower-cost mission capital.⁸³ For enterprises that would be appropriate for CDFI lending but can't be served, lack of access to capital can spell the difference between growth and retraction, hiring and firing, or survival and

⁸¹ Dolan, Cathy. *CDFI Bond: Opportunity of a Decade*. Rep. 2nd ed. Vol. 23. Federal Reserve Bank of San Francisco, 2011. Community Investments. Page 29.

⁸² See footnote 32 above, noting that "overall blended cost of funds for a large [CDFI] loan fund approaches 4 percent in an environment in which banks can borrow long or short-term at a much lower rate, e.g. at 0.25 percent for short-term borrowing." Swack, Michael, Jack Northrup, and Eric Hangen. *CDFI Industry Analysis Summary Report*. Publication. Durham; Carsey Institute, University of New Hampshire, NH. 2012. Page 10.

⁸³ Crowdfunded capital through CDFI Jobs Portals would, we believe, most typically fill financing gaps where CDFI small business borrowers are the issuers with crowdfund investors investing alongside the CDFI co-investors. CDFIs themselves would also have the ability to crowdfund capital directly for on-lending to their borrowers. In this case, the CDFI would be an issuer making an offering on a CDFI Jobs Portal and, to be eligible to make such an offering would need an independent, third party CDFI serving as a co-investor.

failure. From a cost-benefit baseline analysis perspective, we see a marketplace that is underserved due to inefficiencies, insufficient competition in capital supply, and a lack of mission capital formation. In mission-driven crowdfunding, we see a new and significant capital source that can be responsibly channeled through CDFI Jobs Portals to underserved communities in a way that is orderly, efficient, and cost effective.

2. Measuring the Baseline: The Currently Active Non-Securities Crowdfunding Marketplace

Recent crowdfunding successes present a separate and useful baseline by which to measure mission-focused capital formation and the anticipated job creation impact of the CROWDFUND Act. Domestic donation- and reward-based crowdfunding is experiencing substantial year-on-year growth, as is the international securities crowdfunding marketplace.⁸⁴ Rapidly growing market adoption of these models suggests that crowdfunding will become an increasingly significant capital source in many sectors.

We are enthusiastic about the intent of the CROWDFUND Act and the new potential it creates to channel capital towards job creation. And crowdfunding in the U.S. has proven to be a strong new vehicle for raising capital. However, it has proven quite limited in its capacity to create American jobs. The largest crowdfunded projects to date have funded technology peripherals and toys (typically manufactured overseas), and video games⁸⁵ and entertainment (creating jobs in the technology sector, which has high levels of employment in the U.S. and frequently outsources jobs). These types of offerings represent 100% of the Kickstarter offerings that have raised \$1 million or more.⁸⁶

We applaud the success of these startup businesses and initiatives, but they represent just one important way crowdfunding can facilitate capital formation. Another area of opportunity that the SEC can make possible in its rulemaking is capital formation in low-income communities and among populations with high levels of unemployment. We believe the general crowdfunding marketplace is well positioned to facilitate investment in startups and tech-savvy businesses. But to reach local community businesses and social enterprises that may be less tech-savvy, it is the CDFI sector that has shown tremendous success and offers great opportunities. Through CDFI Jobs Portals, CDFIs will enable local enterprises in underfinanced communities across the country to participate in securities crowdfunding and access affordable capital for growth.

While the baseline crowdfunding environment is more oriented towards startups and the technology sector, CDFIs primarily fund more established, local businesses or social enterprises. These local enterprises are often those in “growth mode” and are significant drivers of job growth. Since well-established enterprises financed by CDFIs are more likely to continue to succeed than startups are to achieve success,⁸⁷ CDFIs will help introduce a more stable class of investments to the crowdfunding marketplace.

⁸⁴ Massolution.com. *2013 The Crowdfunding Industry Report*: Massolution, Page 17.

⁸⁵ In 2012, for instance, games were the most popular single crowdfunding category on Kickstarter by both number of supporters and total dollars pledged, at \$83.1 million. Chifkin, Max. "True To Its Roots: Why Kickstarter Won't Sell." *Fast Company*. 18 Mar. 2013. Page 97.

⁸⁶ "Kickstarter." *Stats*. Web. <<http://www.kickstarter.com/help/stats>>. As of June 27, 2013, 25 of the 36 Kickstarter projects to raise more \$1 million or more have been technology related (primarily tech peripherals or video games) and the remaining eleven are in entertainment (including music, comics, tabletop games, and film).

⁸⁷ "Survival of Private Sector Establishments by Opening Year." *U.S. Bureau of Labor Statistics*. 30 Mar. 2012.

B. Assessing the Potential Economic Impact of the Proposed Rules

The discussion below addresses the economic effects of the proposed CDFI Jobs Portal rules, including the likely costs and benefits of the rules, as well as their effect on efficiency, competition and capital formation. Because the proposal involves relaxing some anticipated protections in exchange for alternative investor protections, we also discuss the anticipated costs and benefits of implementing the proposed CDFI Jobs Portal investor protection regime. The subsequent section identifies alternatives to the proposed rules and the costs and benefits of each.

1. Efficiency

CDFI Jobs Portals will create an efficient, fair, orderly and transparent marketplace for mission capital formation.

Once regulations are adopted, crowdfunding will create an entirely new marketplace for investors and issuers of securities. All new offerings will be made available to investors through new funding portals or participating brokers.⁸⁸ Creating an efficient, predictable, and orderly marketplace will be important both for issuers to attract new capital and for investors to successfully identify the investments that best fit their investment objectives.

(a) Efficiency for Investors

For the investor, the proposed CDFI Jobs Portal rule will concentrate a particular type of potential investment (low-return, mission-focused, community development) within a specific type of funding portal. This will likely reduce investor search costs and enhance efficiency. More importantly, the requested exemption from time consuming and burdensome personal disclosures will make the investment process simpler and more efficient, and make mission investor participation more likely. Furthermore, the various investor-protection mechanisms⁸⁹ to be implemented by a CDFI Jobs Portals will help avoid harmful transactions, which cause their own inefficiencies.

(b) Efficiency for Issuers

For the issuer, CDFI Jobs Portals will facilitate simple access to large numbers of mission investors whose small-dollar investments will be efficiently aggregated into simply structured, low-cost loans. These loans will fit seamlessly with issuers' existing CDFI financing. Both of these factors will significantly reduce transaction costs for issuers as compared to the expense of seeking mezzanine financing or other alternative financing.⁹⁰ Capital raising will be far less expensive than engaging in a more traditional and costly securities issuance, such as a private placement under Regulation D.⁹¹ Furthermore, use of a CDFI Jobs Portal will likely be less costly and time consuming than conducting a crowdfunding on a conventional funding portal as it may take more time and effort for a low-return mission offering to raise the requisite amount of low-cost capital when

⁸⁸ Securities Act of 1933, Section 4A (a)(1).

⁸⁹ As detailed above in Section IV.B., Page 15.

⁹⁰ See above in Section V.A.1.(b), Page 22.

⁹¹ See above in Section V.A.1.(b), Page 22.

competing on a site where most investors are more profit-oriented and where competing issuers are (implicitly or explicitly) promoting higher returns.

(c) Regulatory Efficiency

For the SEC, the CDFI Jobs Portal represents an efficient and responsible tool that facilitates a unique and important form of capital formation, protects investors and establishes an orderly, efficient marketplace. The CDFI Jobs Portal does this in a responsible way, with supplementary federal oversight, and always together with financially sound, experienced, and sophisticated CDFI co-investors. Since CDFI Jobs Portals will be subject to Gramm-Leach-Bliley Privacy Rules, they should already meet or exceed whatever privacy standards the SEC establishes pursuant to the privacy provision of the CROWDFUND Act.⁹² In addition, the number of federally regulated 501(c)(3) certified CDFIs is quite small, so the SEC will not need to be concerned with a large marketplace of CDFI Jobs Portals to oversee. These factors assure that the regulatory burden of overseeing CDFI Jobs Portals will be minimal.

(d) Modest Costs of Implementation by Portal

While there are substantial benefits to this approach from an efficiency standpoint, the creators of CDFI Jobs Portals will likely incur higher costs in launching and administering their funding portals due to the more comprehensive investor protection mandates required by the proposed CDFI Jobs Portal rules. That said, CDFI Jobs Portals can rely on structures that are already in place and systems that are relatively easy to implement based on standard practices currently in effect in the CDFI sector. Because CDFI Jobs Portals will be operated by public charities serving a public purpose, higher costs will likely be mitigated by charitable contributions, sales tax exemptions on materials purchases, and an absence of portal investors seeking financial return. From an efficiency perspective, the benefits substantially outweigh the costs.

2. Competition

The CDFI Jobs Portal introduces important and completely new competition with traditional sources of CDFI and low-income community capital. The proposed rule's limitations on rate of return for mission investors⁹³ will create more widely available low-cost capital for issuers achieving charitable impact. The rule thus will introduce a new source of capital for CDFI borrowers to compete with the expensive mezzanine financing and predatory lenders to which these enterprises in low-income communities must often resort for gap financing. It will also allow CDFIs to rely less on their own sources of higher-cost capital, which create little in the way of margin for CDFIs but can be necessary to fully fund transactions. These more expensive sources can instead be replaced with lower-cost crowdfunded participation loans facilitated by CDFI Jobs Portals. More plentiful low-cost capital might also force competing higher-cost sources to lower their rates, which could drive out predatory lenders as well as the higher-cost capital that is more difficult for both CDFIs and community enterprises to afford.

The CDFI Jobs Portal also creates a simple marketplace with universal, "apples to apples" standards for participants and thus facilitates stronger competition among them. Competition is further enhanced by the

⁹² Securities Act of 1933, Section 4A(a)(9).

⁹³ See Appendix A, Rule XX01 (b)(ii)(A).

CDFI Jobs Portal since fraud and failure are better weeded out by its co-investment policies. A more certain marketplace composed of more reliable issuers will bring more participants on the issuer- and investor-side, thus resulting in enhanced competition.

Finally, a CDFI Jobs Portal facilitates competition by serving a sector of businesses that are less tech-savvy, are in communities less accustomed to generating growth through the web, and would be less likely to otherwise participate in the tech-savvy and tech-oriented crowdfunding marketplace. Thus, CDFI Jobs Portals will expand the overall crowdfunding marketplace by attracting issuers who would otherwise be unlikely to participate.

In the context of the securities crowdfunding marketplace, CDFI Jobs Portals may have the competitive advantage of fewer barriers to participation, but they are also subjecting themselves to a series of investor protection standards with which conventional portals will not need or want to comply. Furthermore, we believe that conventional crowdfunding portals and CDFI Jobs Portals will not be direct competitors. They offer different investment products that attract investors with different investment objectives. Conventional and CDFI Jobs Portals may even prove mutually beneficial by increasing interest and participation among different users who come to crowdfunding with differing initial motivations but may begin participating more broadly, thus boosting overall crowdfunding capital formation. In other words, we expect that the capital created through CDFI Job Portals will be additive to the capital created through “conventional” crowdfunding portals. Given the divergent incentives and motivations between profit-maximizing investors and issuers, and mission-driven investors and issuers, we believe that cannibalization is unlikely and that the mission and lower risk offered via a CDFI Jobs Portal will attract many new and different investors to the crowdfunding space. Attracted to the crowdfunding space largely for charitable purposes, many such mission investors may explore profit-maximizing opportunities once they grow comfortable with crowdfunding. In this way, CDFI Jobs Portals may attract new users to the crowdfunding space that conventional portals may not have been able to attract, but from which conventional portals may ultimately benefit, resulting in expanded capital formation.

3. Capital Formation

We estimate the total potential effect on annual capital formation of adopting the proposed CDFI Jobs Portal rules will be \$500 million to \$1 billion⁹⁴ within 3 to 5 years of the rulemaking, as the sector reaches maturity.⁹⁵ This estimate is supported by this section’s summary of the most comparable relevant marketplaces, including (i) the existing crowdfunding marketplace, (ii) the level of investments today by

⁹⁴ This figure refers only to capital raised in the crowdfunding portion of CDFI Jobs Portal transactions, and does not include the co-investment by the CDFI co-investors. CDFI Jobs Portal will make possible many CDFI-funded transactions that would not otherwise be able to successfully close on financing. Because of this fact and because crowdfunded capital will leverage much greater amounts of CDFI capital in most transactions, the total capital formation that the proposed rule facilitates will be substantially higher than the direct crowdfunded securities alone. Here, we limit our analysis to the crowdfunded securities.

⁹⁵ The CDFI sector is quite capable of managing this growth in capital formation. An increase of \$500 million to \$1 billion would represent an increase of 8.3% to 16.7% above the \$6 billion in annual mission finance the CDFI sector currently provides. The capital demand of the CDFI sector and its borrowers is detailed in Section II. F. above, and exceeds the upper end of the CDFI Jobs Portal capital formation totals we project. We note, for instance, that a study of 136 CDFIs, less than 15% of the sector, revealed a capital demand shortfall of \$880 million in a one year period. The sector could capably and effectively deploy this increased volume of capital formation, especially given that growth would likely phase in over three to five years as the CDFI Jobs Portal sector matures.

institutional investors that seek out socially-beneficial investment opportunities, and (iii) the level of investment at international mission crowdfunding sites. Next, we note in this section that as much as 90% of this potential increase could be lost if rules are not adopted to limit the personal disclosure requirements of investors in CDFI crowdfunding investments. Finally, we note that this estimate does not take into account substantial current growth in the broader crowdfunding marketplace, and, as discussed further below, this growth of the crowdfunding marketplace could increase our estimate by a factor of two or more.

(a) Potential Capital Formation Effects of the CDFI Jobs Portal

(i) The Existing Crowdfunding Marketplace

Currently, the domestic crowdfunding sector is made up of two areas of funding activity:

- the regulated peer-to-peer marketplace including the Prosper and Lending Club platforms, and
- non-securities marketplace of donation- and rewards-based crowdfunding which includes sites like DonorsChoose and Kickstarter among many others.

The first primarily attracts investors through the promise of financial return while the second attracts supporters who are primarily passion-driven. CDFI Jobs Portals will combine both of these value propositions, providing both financial return and mission impact as a result of investing.

In 2012, donation and rewards crowdfunding attracted approximately \$1.01 billion in contributions in the United States.⁹⁶ The peer-to-peer lending sector attracted investments in 2012 totaling \$871 million in the United States.⁹⁷ It stands to reason that, at maturity, a sector providing both financial return and mission impact could exceed the two currently active sub-categories in total capital formation. Some considerations, however, mitigate such expectations: the lower rates of return offered by CDFI Jobs Portals and the somewhat narrower set of missions/passions they serve.

CDFI Jobs Portals will typically offer lower rates of return than peer-to-peer lending sites. However, they will offer much higher rates of return than the non-securities space (which can provide only tax deductions or in-kind product rewards) while offering similar mission impact. Furthermore, given that the mission/passion space is larger than the financial return space, one could conclude that mission/passion is a bigger driver of crowdfund investing than is financial return. As to the second mitigating issue, while some donation and rewards crowdfunding is not relevant to the sectors that CDFIs fund, most such crowdfunding is. Furthermore, CDFI Jobs Portals will open crowdfunding into new areas where it is largely inactive, such as small businesses in low-income communities and nonprofits seeking financing. Based on these factors, we feel it is likely the CDFI Jobs Portal space will achieve a scale of capital formation similar to that of the two

⁹⁶ Massolution reports that in 2012 donations and rewards crowdfunding attracted \$1.4B worldwide. Massolution projects that in 2013 72% of crowdfunding will stem from the U.S; it is from this figure that we derived our estimate of total domestic donations and rewards Crowdfunding. (Source: Massolution.com. *2013 The Crowdfunding Industry Report*: Massolution and Drake, David. "U.S. Leads World In Burgeoning Crowdfunding Trend." *Forbes*. *Forbes Magazine*, 12 Apr. 2013. Web.)

⁹⁷ "Lending Club Statistics." Lending Club, 2 Apr. 2013. <<https://www.lendingclub.com/info/demand-and-credit-profile.action>>. "Prosper Performance Data." Prosper, Web. 13 May 2013. <<http://www.prosper.com/invest/performance.aspx>>. We recognize that some of the investment on peer-to-peer sites is placed by institutional investors. We anticipate that institutional investors, such as foundations and institutional impact investors, will also participate as investors on CDFI Jobs Portals.

currently active crowdfunding subcategories and that a range of \$500 million to \$1 billion represents a conservative estimate of that potential scale.

(ii) Sustainable and Responsible Investing

One mission-related financial sector that is already demonstrating both substantial capital formation and recent, rapid growth is the Sustainable and Responsible Investing (SRI) marketplace. This sector “considers environmental, social, and corporate governance criteria (ESG) to generate long-term competitive financial returns and positive societal impact.”⁹⁸

The US SIF (formerly The Forum for Sustainable and Responsible Investment) identified \$3.31 trillion in US assets held at year-end 2011 that apply various ESG criteria.⁹⁹ This market is almost entirely composed of accredited and institutional investors.¹⁰⁰ CDFI Jobs Portals will facilitate mission-related investments that are more direct and broadly accessible by individuals in the U.S. who are not served by investment advisors, or who would prefer more active engagement in mission investing in addition to intermediated SRI investing.¹⁰¹

The SRI marketplace generated \$380 billion average annual growth in new US impact investing between 2009 and 2011.¹⁰² If CDFI Jobs Portals could add to this level of growth by just 0.1% by providing a new, easily accessible method of mission investing to a new population of non-accredited investors, the sector would generate \$380M in new capital.¹⁰³ If CDFI Jobs Portals could further capture just 0.05% to 0.1% of the current-level growth from the existing and rapidly growing impact investing sector (including individual accredited investors), they would attract an additional \$190 million to \$380 million, for a total of \$570 million to \$760 million in crowdfunded mission finance.

(iii) International Mission-Driven Crowdfunding

Kiva and MicroPlace have demonstrated that there is a significant crowdfunding marketplace for mission-motivated online lending. In 2012, these two sites originated approximately \$126 million¹⁰⁴ in debt, the vast

⁹⁸“SRI Basics.” *The Forum for Sustainable and Responsible Investment*. <<http://www.ussif.org/sribasics>>.

⁹⁹ The \$3.31 billion figure does not include shareholder resolutions publicly traded companies from 2010 through 2012. After eliminating overlapping assets involved in both strategies, the total assets for social responsible investment totaled \$3.74 trillion. US SIF Foundation. *Report on Sustainable and Responsible Investing Trends in the United States 2012*. US SIF Foundation, Nov. 2012. Page 11.

¹⁰⁰ Ibid. Page 14. While some impact investment vehicles are marketed directly to non-accredited investors through intermediaries (such as the Calvert Foundation’s Community Investment Note) and while the demand for SRI is growing, the sector remains only indirectly inaccessible to the lower net-worth investor through investment intermediaries such as pension and mutual funds.

¹⁰¹ While the focus of the SRI space is not limited to just the categories of enterprises that CDFIs fund, CDFI Jobs Portals could serve as key platforms for crowdfunding domestic SRI.

¹⁰² As the total US assets in ESG was \$2.55 trillion in 2009, approximately \$760B was added over two years, or approximately \$380B in new investments of funds in this asset class. Ibid., Page 11.

¹⁰³ Achieving this result may be supplemented if lower-income individuals, who donate a larger percentage of their income to charity than do higher-income individuals, show similar behavior pattern when it comes to mission investing. In 2011, the bottom quintile of Americans by income donated and average 3.2% of their income, while the top quintile donated 1.3%. Source: Stern, Ken. “Why the Rich Don’t Give to Charity.” *The Atlantic*. 20 Mar. 2013. Web.

¹⁰⁴ Representing \$115.7 million by Kiva and approximately \$10 million by MicroPlace. Kiva statistics are available at <<http://kiva.org/about/stats>>. The total of \$115.7M is based on historical data from 1/15/12 to 1/16/13. The approximation for MicroPlace is estimated based on the total \$50.14 million lifetime investments (mature and outstanding) funded by MicroPlace from 2007 to 2012, Source: Klein Bier, Jerilyn. “Low-Cost Impact Investing.” *Financial Advisor Magazine*. 28 Sept. 2012. Web.

majority¹⁰⁵ to international microfinance borrowers through field partner intermediaries.¹⁰⁶ The many individual lenders using these sites invest funds in a way that is mission-motivated while providing return of capital.¹⁰⁷ CDFI Jobs portals offer a similar value proposition for U.S. domestic investing, and unlike Kiva will offer modest rates of return.

Because charitable motivation appears to be the major driver of this variety of investment,¹⁰⁸ the ratio of total international to domestic charitable donations allows us to extrapolate from international mission crowdfunding to an estimated future scale of domestic CDFI Jobs Portal crowdfunding. Generally speaking, in the U.S., domestic charitable giving is much higher than giving for causes abroad and we expect that mission investing would follow a similar trend.

According to *Giving USA 2012*, U.S. donors contributed \$22.7 billion to international causes in 2011.¹⁰⁹ By comparison, the *Giving USA 2012* categories for which CDFI Jobs Portals would most typically provide finance – human services, public-society benefit, education and health – represent \$120.4 billion in philanthropic donations domestically, an amount more than five times larger than the international donations.¹¹⁰ Based on this ratio of international to domestic giving, and assuming some similarity between the donation and the mission-motivated-crowdfunding sectors, we can estimate that if international mission crowdfunding attracts \$126 million on an annual basis, the total market for domestic, community development crowdfunding would reach \$668 million per year after three to five years of operation.¹¹¹

(b) Reasonable Assumptions on Platform Performance Support Capital Formation Projections

Based on assessments of analogous fields, we believe that within three to five years of launch, CDFI Jobs Portals can achieve total capital formation of \$500 million to \$1 billion. It is also noteworthy that reasonable assumptions of usage rates and average investment size suggest that this scale is quite attainable. For

¹⁰⁵ With the exception of several recently launched domestic markets, Kiva crowdfunding is mainly limited to the international market. Kiva's important US work is centered around domestic microfinance rather than larger scale community economic development lending proposed here. MicroPlace has historically focused its funding efforts in international lending, and of the current offerings more than half are international.

¹⁰⁶ "About Us." *Kiva*. <<http://www.kiva.org/about>> (2013).

¹⁰⁷ Kiva investors enjoy only return of capital, that is, return of original investment amount while MicroPlace users receive both return of capital and modest rates of return on their investment.

¹⁰⁸ For instance, a University of Michigan study examining motivations of Kiva lenders found that lenders who were motivated by mission factors such as Kiva's unique economic development model and faith-based commitments were more likely to make more loans than lenders driven by any other motivating factor. Liu, Yang, Roy Chen, Yan Chen, Qiaozhu Mei, and Suzy Salib. "I loan because...: understanding motivations for pro-social lending." In *Proceedings of the fifth ACM international conference on Web search and data mining*, pages 503-512. ACM, 2012.

¹⁰⁹ *Giving USA: The Annual Report on Philanthropy for the year 2011* (2012). Chicago: Giving USA Foundation. The category of international affairs includes international development, as well as international relief, international peace, and national security issues as well.

¹¹⁰ *Giving USA: The Annual Report on Philanthropy for the year 2011* (2012). Chicago: Giving USA Foundation. As CDFIs provide loans and other financing to a range of nonprofits and enterprises, the approximate donations to a comparable category includes many different categories of funding. Donations in the types of contribution categories that are relevant for the purpose of this comparison include public society benefits (community and economic development), education (charter schools, early childhood learning, vocation training), health (community health, primary care and advanced care clinics), and human services (affordable housing and shelter, community facilities, vocation training, youth services). CDFIs also provide services to environmental categories (green energy and green retrofitting), and humanities (theaters, arts, and museums), but for the purposes of this analysis are excluded due to their relatively low investment as a representative of CDFI lending finance.

¹¹¹ This analysis is imperfect for a variety of reasons. For instance, the *Giving USA* numbers blend individual and institutional donations. Institutions likely represent a larger percentage of international giving than domestic giving. Furthermore, there are broad sub-categories of international giving that have nothing to do with micro-finance just as there are broad sub-categories of human services, public-society benefit, education and health giving unrelated to community development finance. We hope and expect that the various imperfections offset sufficiently to give a directionally relevant approximation of domestic mission crowdfund investing as compared to international crowdfund investing.

instance, to achieve \$1 billion in capital formation, CDFI Jobs Portals would need to collectively attract 2.5 million users investing an average of \$400/year. With five million investors investing \$100 per year, the portals would raise \$500 million. This user range and average investment is in line with current experience in the crowdfunding marketplace.¹¹²

The table below displays reasonable estimates of the number participating investors and reasonable average investment sizes per investor.¹¹³ Note that items in bold meet or exceed our projected range of capital formation.

Number of Investors

| | | 5MM | 4MM | 3MM | 2MM |
|---------------------------|--------------|-----------------|-----------------|-----------------|-----------------|
| Average Investment | \$400 | \$2 BN | \$1.6 BN | \$1.2 BN | \$800 MM |
| | \$300 | \$1.5 BN | \$1.2 BN | \$900 MM | \$600 MM |
| | \$200 | \$1 BN | \$800 MM | \$600 MM | \$400 MM |
| | \$100 | \$500 MM | \$400 MM | \$300 MM | \$200 MM |

(c) Capital Formation in the Absence of the Proposed Rule

We have asserted that anticipated personal disclosure requirements would substantially discourage mission investor participation, thereby decreasing mission capital formation. The international mission crowdfunding space provides strong evidence of this assertion. The two primary actors differ precisely on this disclosure issue: Kiva does not require substantial personal data disclosures while MicroPlace does. Before investing through MicroPlace, a user must disclose his/her social security number, and self-verify income, liquid net worth, income tax bracket, and investment knowledge and experience. A Kiva investor, by contrast, simply enters his/her credit card number as well as physical and email address, which are customary internet disclosures. As noted above, Kiva facilitates annual originations of \$115.7 million. We estimate MicroPlace facilitates approximately \$10 million, or 8.6% of the total capital formation achieved by Kiva.

Aside from the disclosure requirements, the two organizations are substantially similar. Both are crowdfunding web platforms that facilitate international mission investing.¹¹⁴ Both operate in partnership

¹¹² For instance, in 2012, Kickstarter, the most popular reward crowdfunding site, raised \$320 million from 2.24 million users, representing an average donation of \$160 per user, both numbers we expect to continue to grow. (Source: "Kickstarter." *Stats*. Web. <<http://www.kickstarter.com/help/stats>>) It is reasonable to include that a new sector of financial return-providing CDFI Jobs Portals could exceed the performance of a single site, notwithstanding the fact that it is popular a popular one. The average Kiva investor has invested \$467 on the site in total. MicroPlace, which offers return similar to that projected for CDFI Jobs Portals, achieves an estimated average investment size of \$3,850 per user over time on their site. Data on average number of years investors are active on Kiva and MicroPlace is not available to precisely calculate an average annual investment amount. The average lifetime investment per MicroPlace user is calculated by using the total amount of MicroPlace originated loans form 2007-2012 (\$50,140,000) divided by the total number of investors during that same period (13,000). Source: Klein Bier, Jerilyn. "Low-Cost Impact Investing." *Financial Advisor Magazine*. 28 Sept. 2012. Web. Kiva's average lifetime investment per Kiva user is found using the total amount of Kiva originated loans (\$439,868,875), divided by the total number of lenders (941,956) during the same period. Source: "Kiva - About Us." *Kiva - Stats*. Data from up to 08 June 2013. <<http://www.kiva.org/about/stats>>.

¹¹³ With median investment of \$900 million and a mean investment of \$875 million.

with established and respected local microfinance agencies, through which they channel capital to borrowers. (The only other significant difference between the two sites would seem to favor MicroPlace, because Kiva provides only return of original investment while MicroPlace is a registered broker dealer offering low rates of return in addition to return of investment. The lesson here suggests that in the mission crowdfunding space, the promise of financial return alone has not been sufficient to make up for the barrier of personal data disclosures.¹¹⁵)

The similarity of these two mission-driven crowdfunding platforms, Kiva and MicroPlace, allows us to isolate the variable of personal disclosures and the impact of these disclosure requirements on capital formation. In this real-world example, we see an 11.5x advantage for a comparable site offering fewer barriers to participation. Extrapolating from this, and conservatively assuming a 10x advantage in the absence of personal disclosure requirements, we would expect the above-projected \$500 million to \$1 billion annual mission capital formation to drop by 90%, achieving only \$50 million to \$100 million in capital formation in low-income communities if significant disclosures were required. Thus, in absence of the proposed CDFI Jobs Portal rule, we would expect to sacrifice \$450 million to \$900 million in mission finance each year. Of course, the actual capital formation impact may be even more severe, as the smaller potential for capital formation would likely decrease the appeal of the crowdfunding marketplace to CDFIs, likely resulting in little participation, a lower level of investment in the quality of platforms which will be less likely to financially sustain themselves, and a less robust marketplace. Note also that the leveraging effect, through which crowdfunded capital would make possible substantially larger CDFI investments in transactions, would also be largely sacrificed.

(d) Crowdfunding Sector Growth Is Likely to Amplify These Projections

The preceding capital formation projections may be viewed as conservative because they exclude consideration of the fact that the crowdfunding sector has been growing rapidly and is projected to continue to do so as more and more investors become accustomed to this new approach to investing.

Massolution's crowdfunding report finds total worldwide crowdfunding to have grown 81% in 2012.¹¹⁶ Deloitte's *Technology, Media, and Telecommunications Projections 2013* state that the crowdfunding sector is growing at more than 50% a year.¹¹⁷

¹¹⁴ While Kiva was the first mover in the space, MicroPlace was launched within two years of Kiva, in 2007, and is owned by eBay, providing a resource and experience advantage that the start-up Kiva does not enjoy.

¹¹⁵ Of the two core differences between Kiva and MicroPlace, disclosure requirements and provision of financial return, it is unlikely that the latter explains the lower capital formation performance of MicroPlace. To the contrary, the potential for financial return likely increases the participation MicroPlace achieves. There is ample evidence of mission-investor demand for financial return as indicated, for instance, by sizable and growing SRI marketplace detailed above. Further, as indicated by the peer-to-peer lending space (also detailed above), we know that crowdfunding investors display demand for financial return. With demand for return well-established in the mission investing space (SRI) as well as the crowdfunding space (peer-to-peer lending sites), it is not likely that the linking of crowdfunded mission investing with financial return is the cause of the substantial capital formation difference between Kiva and MicroPlace. Given this (and given that MicroPlace's backing by the highly successful web enterprise PayPal suggests that inexperience or lack of resources for growth is not the cause of the underperformance), it is highly likely that the barriers to participation presented by personal disclosure requirements explain comparative capital formation differential between the two sites.

¹¹⁶ Massolution.com. *2013 The Crowdfunding Industry Report*: Massolution.

¹¹⁷ Rep: Deloitte. Page 17.

Within three to five years, the size of the overall sector could quite possibly double or more, driven by broader market adoption of crowdfunding. Such growth will likely be experienced proportionally by CDFI Jobs Portals and so the total capital formation as a result of proposed rule, would be substantially higher than those projected here. Based on our present-day estimates of \$500 million to \$1 billion, with sector-wide annual growth of 30% over three years, CDFI Jobs Portals could achieve \$1.1 billion to \$2.2 billion in annual capital formation.

C. Alternatives to the Proposed Rule

There are a number of alternatives to the proposed CDFI Jobs Portal solution that the SEC might consider in promulgating the regulations governing the CROWDFUND Act. Below we outline the most plausible alternatives and review the benefits and costs associated with each as compared to the proposed rules.

1. Do Not Accommodate Mission Capital Formation

As detailed above,¹¹⁸ anticipated barriers in the implementing rules may severely limit the otherwise strong potential of securities crowdfunding as an efficient and substantial source of mission capital for disinvested communities. The proposed rules will remove these barriers while adding a stronger set of investor protections than contemplated by the law. One alternative to this approach would be for the SEC to produce regulations that make no special effort to facilitate mission capital formation. This alternative would be the most logical outcome if the regulations are developed without recognizing the differing motivations and behaviors when individuals make profit-maximizing versus mission investments.¹¹⁹ The benefit of this approach is that it may save regulatory costs; however, the structure of the proposed rules – involving a small, tightly defined group of funding portals subject to oversight by an additional financial institution regulator and offering a series of strong investor protection mechanisms – suggests that the incremental cost to the SEC from adopting the proposed rules would be minimal. Of course, the costs of not adopting rules that reduce barriers for mission capital formation would mean missing an opportunity to introduce a practical and responsible approach to channel affordable capital to the enterprises serving communities that need it most.

2. Minimize Barriers for All Investors

The Commission could also reduce investor barriers by introducing regulations that require minimal personal disclosures for all investors, such as a checkbox to verify compliance with the law's income-based investment limits. The rules could further be very permissive about the CROWDFUND Act's advertising restrictions. Such a solution would address the concerns we pose with respect to mission investor participation by removing anticipated barriers for all crowdfunding investors. One benefit of this approach may include lower initial regulatory cost since standards to enforce would be minimal. Another may be higher initial capital formation since low barriers to usage would attract more participants. It is also likely that average investment size would be larger, further increasing the amount of capital formation, though this effect would stem primarily from the ability to easily circumvent the statutorily mandated investment limits. It appears that Congress

¹¹⁸ See above, Section III. A, page 10 and Section III.B., page 12.

¹¹⁹ As noted above, individuals who engage in mission investing almost always also engage in profit maximizing investing, although typically display different investment behavior based on the type of investment.

intended to facilitate crowdfunded capital formation while ensuring through income- and wealth-based investment ceilings that no investor put too much at risk in crowdfunding investments. Balancing these objectives is among the most challenging tasks the SEC faces in this rulemaking.

The Commission has received an abundance of advice on these matters from the crowdfunding community as well as from investor protection advocates and securities experts. Some argue that the wisdom of the crowd will mitigate investment risks and counsel in favor of minimal restrictions in order to facilitate greater capital formation. Others suggest that startup-business failure rates and risks of fraud will lead to financial loss, and thus advocate for rigorous investor protections.

We do not take a position on the appropriate level of personal disclosure standards for portals that are not CDFI Jobs Portals, and recognize there are strong opinions on both sides. We do recommend, as detailed in the following section, that the investor disclosure standards should be consistent across investment amounts unless the lower disclosure standards are accompanied by strong alternative protections such as those proposed herein.

3. Exempt All Small Dollar Investors

Recognizing that by definition small dollar investments involve lower exposure, the Commission could exempt all individual investments from personal disclosures up to some maximum such as \$200 or \$500 on the grounds that even if the risk of failure and fraud were high, exposure would be low. Similar in effect, the SEC could establish a low-barrier “check the box” system for these smaller investments.

The key benefit of this approach, should the SEC determine it is so authorized under Title III, would be greater aggregate capital formation as a result of a larger number of small investors funding more offerings. However, since the dollar amounts are low, even in the aggregate, the capital formation upside may not be worth the regulatory enforcement and investor protection costs.

An uneven disclosure standard based on investment size would have the effect that a larger number of crowdfunding investments would come in very small dollar amounts. Investor protection advocates suggest that this approach presents an unacceptable potential for fraud, as fraudulent issuers may see a special opportunity to raise substantial amounts by aggregating \$200 investments from thousands of investors, knowing that (i) many such investors are likely to be unconcerned with the small loss or may fail to investigate how the issuer actually uses the funds raised¹²⁰ and that (ii) other small dollar investors, expecting returns a few years in the future, may simply forget they’ve made a small investment in the first place. For many investors, this may be a relatively unimportant concern and may present an acceptable risk.

In providing broad disclosure exemptions for small-dollar investments versus larger investments, the SEC may see particular risk for low-income individuals in low-wealth communities who can least afford to lose what wealthier individuals might see as inconsequential amounts. Low-income individuals and communities

¹²⁰ See e.g. “The Great Crowdfunding Train Wreck of 2013.” Antone Johnson, *Mashtag Blog*, 22 Mar. 2012.

would disproportionately provide these small dollar investments and we are aware of the SEC's findings that low-income and minority communities are more often targets of investor abuses and scams.¹²¹ Given the high levels of fraud in vulnerable communities, we are concerned that the low-income constituency whose wealth the CDFI sector seeks to build could be compromised by disclosure requirements that vary based on investment amount.

We note that small dollar investments will represent a more significant portion of low-income individuals' wealth and income than for other investors. As a result, permitting lower participation barriers for all small dollar investments would effectively reduce protections for most any crowdfunded investment a low-income individual would have the financial capacity to make. The effect of this would be that a vulnerable subset of the population – low-income individuals who can least afford financial loss – would essentially be assigned to the riskiest portion of the market with the fewest restrictions and the portion of the market that some contend is the highest risk for fraud and abuse. This concern only becomes more acute when one considers, as noted above, that low-income communities are more frequently victims of affinity fraud and Ponzi schemes.¹²² In an era of broad online access, a crowdfunding portal with low barriers to entry for smaller investments could be an effective and scalable new tool to perpetrate frauds that the SEC has concluded are already far too common in low-wealth and minority communities. Given that 20% of the nation's population earns less than \$20,000 a year¹²³ – a group that includes low-income community residents, the disabled and retirees – one can see that deep negative impacts on individuals could also be broadly felt nationwide.

Furthermore, uneven requirements based on investment size may have the effect of driving a very large number of micro-investments, including vast numbers of five and ten dollar investments. As a result, the SEC may incur substantial enforcement and regulatory costs in order to enable investments that will ultimately generate only a small percentage of total crowdfunded capital formation.

Broadly exempting small-dollar investments from investor disclosures may also make it difficult for the SEC to enforce the statutory limitation on an investor's total crowdfunding investments.¹²⁴ While investment on any one portal may be limited, investors could easily (either intentionally or unintentionally) exceed the total investment limits (or be coerced into doing so) by investing small amounts across multiple portals. By contrast, the proposed CDFI Jobs Portal rules are designed to prevent investment beyond the statutory maximums. Since only a small number of federally regulated entities would be eligible to create a CDFI Jobs Portal, the number of potential portals in the marketplace would be very small. As detailed in the draft

¹²¹ "Affinity Fraud: How To Avoid Investment Scams That Target Groups." Securities and Exchange Commission. *Investor Alert: Affinity Fraud*. Web. A serious concern is the potential for community-based issuers to exploit their affinity networks and trust within their communities to raise fraudulent issuances in the practice of affinity fraudsters or community Ponzi schemes. The SEC defines affinity fraud as "investment scams that prey upon members of identifiable groups, such as religious or ethnic communities, the elderly, or professional groups." Nearly one in four Ponzi schemes utilizes affinity-group tactics, and the most common affinity group targets are elderly or retired individuals, religious groups, and ethnic groups. (Source: "The Marquet Report on Ponzi Schemes." *Marquet International*, 2 June 2011.) Given the historical precedent for affinity frauds and Ponzi schemes to prey on members of their own communities, the investor protection guidelines found in our recommended rule present multiple steps of barriers and deterrents from the proposed rules from being used to perpetuate affinity fraud.

¹²² Ibid.

¹²³ United States. Congressional Research Service. *The Distribution of Household Income and the Middle Class*. By Linda Levine. Washington, DC: Congressional Research Service, Library of Congress, 2011.

¹²⁴ Securities Act of 1933, Section 4(a)(6)(B).

rule,¹²⁵ CDFI Jobs Portals will take steps to ensure that no investors exceed the universal \$2,000 limit across all portals¹²⁶ without verifying their ability to do so by virtue of their income or net worth. CDFI Jobs Portals would do this by sharing available identifying data such as names and addresses, a task made easier since the total number of portals will be small.

Furthermore, if barriers to entry were low across the small-dollar crowdfunding marketplace regardless of level of investor protection, CDFIs taking extra steps to ensure responsible lending would find themselves at a competitive disadvantage. While the costs of implementing the CDFI Jobs Portal may be low, there would be little incentive for a CDFI Jobs Portal to incur the costs of its investor protection approach if investors could enjoy the same “low-barrier” convenience from portals that do not take similar steps to protect them. If disclosure standards are uneven without offsetting alternative investor protections, the ultimate effect could be a “race to the bottom” for investor protection standards in the small-dollar crowdfunding marketplace.

For these reasons, and recognizing that that the impact of risk-taking on a family has less to do with the size of an investment than it does with the share of household income or assets that investment represents, adopting disclosure requirements that are consistent across investment amounts will help limit disproportionate low-income investor exposure. In the absence of strong substitute investor protection mechanisms that can be reliably enforced by a portal such as those recommended above, applying uneven disclosure requirements based on investment size may likely introduce more costs than benefits, resulting in a less fair, less efficient, less orderly marketplace.

4. Exempt All Issuances Involving Co-Investments

Recognizing that transactions are much less likely to involve fraud and more likely to be successful with a sophisticated co-investor, the SEC could remove or lower investor barriers whenever such a co-investor is involved in a securities crowdfunding transaction. A clear benefit of this approach is that it would encourage greater capital formation through the CROWDFUND Act while better protecting investors.

Such a rulemaking would likely involve defining which co-investor types qualify to co-invest with crowdfunding investors on portals that have lower-barriers to participation. A potential cost would be ensuring that such co-investors operate responsibly and verifiably co-invest real funds. Though it would come at some cost, the SEC may find it valuable to implement quality control standards for applicable co-investors and perhaps revoke participation rights from those that too frequently incur losses for crowdfunding investors. Such a function could also be carried out by an independent funding portal. If such co-investment structures were facilitated by a large number of funding portals along with an exemption from personal disclosure requirements, another potential cost is that it would become easier for investors to intentionally or unintentionally exceed the law’s mandated investment limits (assuming such portals also included an exemption from personal disclosure data tracking). For this reason, the SEC may want to set

¹²⁵ See Appendix A, Rule XX01, (a)(ii)(A)(II).

¹²⁶ Any CDFI Jobs Portal should be enabled to easily link to any broader cross-portal exchange or other mechanism mandated by the SEC to make reasonable efforts to ensure investors have not exceeded the \$2,000 between conventional and Jobs Portal crowdfunding.

standards that effectively limit the number of potential funding portals that could operate in this area. Such entities should be able to communicate with one another easily to prevent investors from exceeding limits, by sharing available identifying data such as names and addresses, as would be the case for CDFI Jobs Portals.¹²⁷ It is conceivable that a CDFI Jobs Portal could responsibly implement such a co-investor approval and information sharing platform since it would already have systems in place for co-investor quality control and inter-Jobs-Portal data sharing between portals¹²⁸ and would also already be subject to Gramm-Leach-Bliley privacy rules and independent federal regulatory oversight.

5. Variations on the CDFI Jobs Portal Approach

If the SEC sought to specifically accommodate mission investors and to facilitate this especially promising area of capital formation, there are a number of plausible iterations to the proposed CDFI crowdfunding rules. We outline two possible approaches, the first more permissive – expanding the footprint of CDFI Jobs Portals – and the second alternative more tightly limiting CDFI Jobs Portals’ range of authority.

(a) Implement CDFI Jobs Portal Rules That Permit Co-Investors Beyond CDFIs

The SEC could value the co-investor quality control, privacy protections, and charitable focus of the CDFI Jobs Portal approach and seek to expand further the mission capital formation these funding portals facilitate by permitting co-investors beyond CDFIs. Such an approach could specifically define the broader universe of permitted mission-oriented co-investors to include:

- SBA lenders,
- charitable private foundations, and
- conventional financial institutions originating Community Reinvestment Act-qualifying loans.

Alternatively, the SEC could grant qualifying CDFI Jobs Portals independent authority to define what co-investors qualify to participate.

Expanding the field of participants to other mission-oriented co-investors within the CDFI Jobs Portal structure would allow the SEC to rely on its longstanding exemptive preference while further increasing charitable capital formation. While this would broaden the population of co-investors (and, as a result, issuers), the platform on which the offerings post would be on CDFI Jobs Portals, and so would maintain the proposed series of investor protections that CDFI Jobs Portals will provide. The clear benefit of such an approach would be to significantly increase mission capital formation, expanding the impact of a low-cost, well-conceived exemption that protects investors. To the extent the Commission prefers a more cautious initial approach in creating CDFI crowdfunding portal rules, it may prefer to limit participation to CDFIs alone. The SEC may perhaps consider an expansion of permitted co-investors upon substantial evidence of successful capital formation and investor protection in the more tightly-defined CDFI Jobs Portal rules recommended in this letter.

¹²⁷ As noted above, the collection and tracking of names and addresses would likely be the primary way in which CDFI Jobs Portals complied with the proposed provision in Appendix A at (a)(ii)(A)(I) and (a)(ii)(A)(II).

¹²⁸ In order to comply with Rule (a)(ii)(A)(I) in Appendix A.

(b) Implement CDFI Jobs Portal Concept, But Limit to Issuers That Are Charities

The 501(c)(3) CDFI Jobs Portal facilitates charitable impact regardless of whether the issuer itself is a charity. Recognizing that intended charitable impacts – such as community development and job creation in underserved communities – can be produced by for-profit and nonprofit issuers alike, the fact that the co-investors are established CDFIs is sufficient for charitable purposes.

That said, in creating rules that involve special exemptions, the Commission may prefer that participation be more strictly limited to an issuer type for which there is specific, longstanding precedent of granting exemptive relief: 501(c)(3) charities. Such a scenario would provide the Commission the investor protection assurance of the CDFI Jobs Portal while limiting the possible market of issuers to 501(c)(3)s only. The inverse of the solution proposed in Section 5.(a) above, this approach would substantially limit the range and number of possible issuers participating through the CDFI Jobs Portal exemption and thus reduce total mission capital formation, mission impact, and job creation.

VI. Conclusion

Lack of sufficient capital is a primary impediment to job creation in low-income communities. Access to crowdfunded capital from mission investors through CDFI Jobs Portals would allow CDFIs to channel substantially more capital towards job creation in these disinvested communities. We write in support of a solution that would facilitate the deployment of mission investor dollars towards job creation in low-income communities through the unrivaled capacities and proven impact of CDFIs.

The SEC's rulemaking will be critical in determining the extent to which the legislation achieves its objective of creating jobs while protecting investors. We strongly encourage that the law's core intended outcome of job creation be responsibly inclusive of the underinvested, low-income communities where unemployment is high and jobs are needed most. At the same time, we want to ensure that investors, especially those in the vulnerable communities CDFIs serve, are protected.

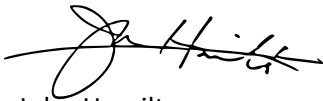
The proposed CDFI Jobs Portal rules will enhance investor protection and mission capital formation. CDFIs are uniquely well positioned to responsibly channel crowdfunded investment towards the charitable purpose of creating jobs in areas that need it most. To make possible implementing rules that encourage greater mission investor participation – including more permissive income/asset verification standards and the ability to promote mission elements of transactions – CDFI Jobs Portals and their participants will be subject to a series of new investor protections that are more stringent than those required by law but that do not present barriers for mission capital formation. In adopting the proposed rules, the SEC will ensure that the crowdfunding rules reflect its own longstanding policy of providing responsible exemptive relief in service of the public interest.

In his Statement for the Record, CROWDFUND Act co-author, Senator Merkley encouraged the SEC staff developing the regulations to consult with the Treasury Department's CDFI Fund.¹²⁹ We also encourage the Commission to contact and discuss the proposed rules and their alternatives with the CDFI Fund, which can provide insight on CDFI sector performance, scale, capital needs, and expertise in channeling capital to underinvested communities.

Thank you for your consideration. If you have any questions regarding the contents of this letter, or would like to contact us, please do not hesitate to do so at:

info@cfenterprises.org
(202) 745-4486

Sincerely,

A handwritten signature in black ink, appearing to read "John Hamilton", with a stylized flourish at the end.

John Hamilton
President, City First Enterprises

¹²⁹ Senator Jeff Merkley (OR). "Crowdfunding." *Congressional Record* 158:113 (July 26, 2012) page S5474.

Appendix A: CDFI Jobs Portals – Rulemaking Recommendations

Recommended rules for offerings made through CDFI Jobs Portals pursuant to Section 302 of the Jumpstart Our Business Startups (JOBS) Act.

CDFI Jobs Portal

SECURITIES ACT RULES

DEFINITIONS (*to be inserted into definitions applicable to crowdfunding rules generally or could be included as the first subsection of the rule text below*):

(a) *CDFI*. “CDFI” means any person that has been certified, and has not been decertified, as a Community Development Financial Institution by the United States Department of the Treasury’s Community Development Financial Institutions Fund, pursuant to 12 CFR 1805.201.

(b) *CDFI Jobs Portal*. “CDFI Jobs Portal” means a funding portal that

- (i) is, or is controlled by, a CDFI that is recognized by the Internal Revenue Service as being (A) exempt from United States federal income tax by reason of sections 501(a) and 501(c)(3) of the Internal Revenue Code and (B) a public charity;
- (ii) is subject to oversight, supervision or regulation by a Federal banking agency, as that term is defined in section 3(z) of the Federal Deposit Insurance Act;¹ and
- (iii) has registered with the Commission and the applicable self-regulatory organization as a CDFI Jobs Portal.²

(c) *Qualified co-investor*. “Qualified co-investor” means a person that

- (i) is a CDFI;
- (ii) satisfies the standards established by a CDFI Jobs Portal pursuant to Rule XX01(b)(i)(A); and
- (iii) co-invests in a CDFI crowdfunding transaction pursuant to paragraph Rule XX01(b)(ii)(B).

¹ The definition of “Federal banking agency” cross-references the Federal Deposit Insurance Act definition of the term, which includes the Federal Reserve Board, the Office of the Comptroller of the Currency and the Federal Deposit Insurance Corporation. The use of “oversight, supervision or regulation” is intended to cover insured depository institutions and their holding companies, as well as all entities controlled by either, as determined under the applicable rules of the appropriate Federal banking agency.

² We would propose that the registration provisions for funding portals that the Commission adopts pursuant to Section 4A(a)(1) of the Securities Act permit a funding portal to check a box identifying itself as a CDFI Jobs Portal.

To be inserted as a rule within the crowdfunding regulations:

Rule XX01. CDFI Crowdfunding Transactions.

(a) *General.* The provisions of this paragraph (a) shall apply to [crowdfunding transactions]³ that satisfy the conditions of paragraph (b) of this Rule XX01.

(i) *Integration.* Offers and sales made to a qualified co-investor in a transaction pursuant to this Rule XX01 will not be considered part of the offering pursuant to this Rule XX01.

(ii) *Investment limits and investor tracking.*

(A) Each investor may invest up to \$500 in an offering pursuant to Rule XX01 without affirmatively verifying their income and identity as otherwise required in [section of the regulations that sets forth income and identity verification requirements], provided that the CDFI Jobs Portal arranging such offering takes efforts, with respect to each investor in the offering whose income and identity is not verified, to:

(I) ensure that such investor in a 12-month period has not purchased securities offered pursuant to Rule XX01 that, in the aggregate, from all issuers, exceed \$500; and

(II) ensure such investor in a 12-month period has not purchased securities offered pursuant to Section 4(6) of the Securities Act, in the aggregate, from all issuers, exceeding \$2,000.

(B) Each investor in an offering pursuant to Rule XX01 that has affirmatively verified their income or net worth as set forth in [section of the final regulations that sets forth income and identity verification requirements] will be subject to [section of the final regulations that set forth requirements preventing investors from exceeding annual investment limits].

(iii) *Communications.*

(A) A notice,⁴ circular, advertisement, letter, sign or other communication, published or transmitted by the issuer to any person, which refers to any offering of securities pursuant to this Rule XX01 will not be deemed to be an advertisement of the terms of the offering for purposes of Section 4A(b)(2) of the Act, *provided* that the communication contains no more than the following:

³ We have used “crowdfunding transactions” to refer to a transaction that is exempt pursuant to Sec. 4(6) under the Securities Act pursuant to rules to be adopted by the Commission.

⁴ Alternatively, this may be included as a new Rule 135f.

- (I) a description of the non-financial, charitable aspects of each offering;⁵
- (II) images, photographs or other graphic material reflecting non-financial, charitable aspects or each offering;
- (II) a statement that the offering is a mission investment offering below market rates of return;
- (III) information identifying the CDFI Jobs Portal, the qualified co-investor, and the issuer;
- (IV) the URL at which the offering can be found;
- (V) [any relevant advertising permissions granted broadly to other funding portals]; and
- (VI) [any legends or other information deemed necessary or appropriate by the Commission].

(B) A CDFI Jobs Portal or a qualified co-investor shall not be deemed to be an “issuer” within the meaning of Section 4A(b)(3) if it publishes or transmits a communication meeting the requirements of paragraph (a)(iii)(A) of this Rule XX01.

(iv) *Presentation of Offerings on CDFI Jobs Portal.* A CDFI Jobs Portal may structure, order, categorize, present, make searchable, and otherwise organize offerings under this Rule XX01 in any way that it deems appropriate in its own discretion, to best achieve its charitable and mission capital formation goals, without any priority given to a particular offering being deemed compensation under Sec. 4A(b)(3) of the Securities Act, *provided* that the CDFI Jobs Portal does not give greater prominence to any offering on the basis of the consideration received or to be received by it in its capacity as the CDFI Jobs Portal with respect to such offering.

(b) *Conditions to be Met.*

(i) *Obligations of CDFI Jobs Portal.* With respect to a securities offering pursuant to this Rule XX01, the CDFI Jobs Portal acting as intermediary in such offering must:

(A) Establish publicly disclosed standards to serve as a qualified co-investor in offerings pursuant to this Rule XX01 in which the CDFI Jobs Portal acts as intermediary; such requirements, at minimum, must include: verifiable standards relating to financial stability and strong loan performance;

(B) Annually verify the status of the qualified co-investor under this Rule XX01 and under the standards established by the CDFI Jobs Portal pursuant to paragraph (b)(i)(A) of this Rule XX01;

(C) Ensure that each investor positively affirms that the investor is making a mission investment offering below market rates of return; and

(D) Ensure that the offering complies with paragraph (b) of this Rule XX01.

⁵ No such advertisement may include reference to any financial term of the offering including offering size, investment size, rate of return, tenure, or any other term or financial aspect of the offering.

(ii) *Transaction Requirements.* A transaction pursuant to this Rule XX01 must, at minimum, include:

(A) Crowdfunding securities. The securities offered must be limited to non-convertible debt securities offering interest-based return of 5 percent or less;

(B) Issuer's investment. The issuer must make a contribution in the form of equity or other issuer resources, as shall be approved and verified by the qualified co-investor, which issuer's investment / contribution must be in first-loss position with respect to all other investors in the Transaction; and

(C) Investment by qualified co-investor. A qualified co-investor must make an investment that is not part of the crowdfunded offering.⁶

(D) Disclosure. The terms of co-investments pursuant to paragraph (b)(ii)(C) of this Rule XX01 and issuer investment pursuant to paragraph (b)(ii)(B) of this Rule XX01 must be disclosed on the CDFI Jobs Portal.⁷

EXCHANGE ACT RULE

Rule 3a80-1. Advertising of Charitable Aspects by CDFI Jobs Portals

A person that acts as an intermediary in a transaction involving the offer or sale of securities for the account of others pursuant to Section 4(6) of the Securities Act of 1933 shall not be deemed "to offer investment advice or recommendations" or "to solicit purchases, sales or offers to buy the securities offered or displayed on its website or portal" within the meaning of Section 3(a)(80) of the Securities Act if, in connection with an offering by an issuer in reliance on Rule XX01 of the Securities Act, such person issues any notice, circular, advertisement, letter, sign or other communication, which refers to such offering, *provided* that the communication contains no more than the information set forth in Rule XX01(a)(iii)(A) under the Securities Act.

INVESTMENT ADVISERS ACT

Although we propose that to require a co-investment by a qualified co-investor as a condition to the exemption from certain aspects of the crowdfunding rules, in the belief that a qualified co-investor's due diligence will decrease incidences of fraud and benefit crowdfunding investors in other ways, we request that either the regulatory text (for example, a new Rule 202(a)(11)(H)-1 under the Investment Advisers Act) or guidance contained in the adopting release should make clear that a qualified co-investor will not be

⁶ This investment may be a bank loan or credit facility or securities that are offered in a registered offering or pursuant to an exemption from registration such as Section 4(2) or Regulation D.

⁷ We would propose that this disclosure requirement be included, with respect to offerings conducted pursuant to this Rule XX01, as a required item in the disclosures that the Commission adopts pursuant to Section 4A(b)(1) of the Securities Act.

deemed an Investment Adviser by reason of its activities undertaken in connection with the transaction in compliance with Rule XX01 under the Securities Act, including promoting the non-financial, charitable aspects of an offering in communications pursuant to Rule XX01(a)(iii)(B); or being identified as the qualified co-investor by the issuer or the CDFI Jobs Portal in marketing materials and on the CDFI Jobs Portal listing or providing technical assistance to issuers in connection with a crowdfunding offering. Similarly, we request that the release make clear that a CDFI Jobs Portal will not be deemed to be an investment adviser if it promotes the non-financial, charitable aspects of an offering in compliance with Rule XX01(a)(iii)(B) or providing technical assistance to issuers in connection with a crowdfunding offering.