

MEMORANDUM

FROM: Sebastian Gomez Abero
Special Counsel
Office of Chief Counsel, Division of Corporation Finance
U.S. Securities and Exchange Commission

RE: Meeting with representatives of City First Enterprises

DATE: July 30, 2013

On July 23, 2013, Commission staff met with representatives of City First Enterprises to discuss issues regarding the implementation of Title III of the Jumpstart Our Business Startups Act.

The following Commission staff were present: Tamara Brightwell from the Office of the Chairman; Keith Higgins, Jennifer Riegel and Sebastian Gomez Abero from the Division of Corporation Finance; and David Blass and Leila Bham from the Division of Trading and Markets.

The following representatives from City First Enterprises were present: John Hamilton, Dave Wilkinson, Suzanne Adatto and John Olson (Gibson, Dunn & Crutcher).

The information provided by the representatives of City First Enterprises is attached.

Attachment

Securities Crowdfunding and the CDFI Jobs Portal: Increasing Mission Capital Formation while Protecting Investors

In April 2012, Congress passed the JOBS Act, including Title III, which creates a new exemption from registration of securities sold via crowdfunding when certain criteria are met. We seek 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 document outlines a solution that will increase job-creating mission capital formation while enhancing investor protections.

Mission Investors, the CROWDFUND Act and Job Creation

Mission investing could substantially contribute to the law's intent of channeling new capital towards the creation of jobs, particularly in underinvested communities. There is, however, 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.

We recognize that it is necessary for the SEC to develop rules that strike a balance between capital formation and investor protection. We support a solution that will provide an alternative set of investor protections stronger than those called for in the law while avoiding otherwise-anticipated barriers to mission investor participation.

We propose rules that engage the expertise of U.S. Treasury-certified Community Development Financial Institutions (CDFIs) as co-investors in crowdfunding transactions to substantially reduce risk of fraud and loss. Rules for mission investors would be carried out by a new type of crowdfunding portal called CDFI Jobs Portals which will establish an orderly, efficient marketplace that facilitates the formation of mission-driven capital at scale. CDFI Jobs Portals will implement a series of investor protections, thereby enhancing the quality of investments offered.

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. There are over 1,000 CDFIs managing \$64 billion in assets and originating \$6 billion a year in underinvested communities nationwide.

Inadequate access to capital for CDFIs and their borrowers is a major impediment to achieving even greater job creation and community impact. At the same time, there are currently no efficient ways for small-dollar mission investors to invest in community enterprises. Mission-driven crowdfunding represents a solution to this problem. Crowdfunded capital can be co-invested alongside CDFI

dollars, filling financing gaps that often prevent mission transactions from coming together. The result will be a significant new marketplace for responsibly channeling capital that generates jobs and economic development at scale.

The Challenge within the CROWDFUND Act

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:

- (1) Income and/or asset verification requirements for mission investors (who will typically invest small amounts) may prove overly burdensome.
- (2) Marketing limitations would substantially reduce the ability to inform mission investors of impact investment opportunities.

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. CDFI Jobs Portals and their participants would be subject to a series of supplementary investor protections more stringent than those required by the law, as summarized below.

Investor Protections Extended Through the CDFI Jobs Portal vs Anticipated Rules for Standard Portals

CDFI Jobs Portal Participation Requirements	Jobs Portal	Standard Portal
CDFI co-investment An issuer must have attracted a co-investment from a qualified CDFI in the same transaction.	Yes	No
Strict standards & ongoing quality control of CDFI co-investors Co-investing CDFIs must meet high performance standards relating to loan loss rates, reserves, and capitalization.	Yes	No
Issuer "skin in the game" Each issuer must invest or put at risk its own resources.	Yes	No
Restricted to lower-risk loans with low rates of return Offerings are restricted to low-yield debt securities, thereby eliminating any "get-rich-quick" temptation on the part of investors.	Yes	No
Proven financial strength overseen by Federal regulators CDFI Jobs Portals must be controlled by regulated financial institutions, subjecting them to oversight by federal banking regulators.	Yes	No
Subject to Gramm-Leach-Bliley privacy rules As federally regulated financial institutions, CDFI Jobs Portals will be subject to GLB privacy rules, thereby easily meeting Title III's privacy protection mandate.	Yes	No
Investor personal data disclosure for tracking maximum aggregate crowdfunding investment	Over \$500: Yes \$500 or less: No	Yes

Permission for CDFI Jobs Portals

We believe this series of requirements, taken together, creates an investor protection regime stronger than that required under the Title III. In light of these supplementary protections and unique opportunity to drive mission capital formation, we recommend that, in case of CDFI Job Portals, 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.
- *Permit Categorizing, Searching and Featuring:* Enable mission investors to easily identify the causes they support by permitting categorization based on non-financial, mission elements of posted offerings.
- *Permit the use of Credit Cards:* Facilitate ease of investment by allowing CDFI Jobs Portal Mission Investors to make investments using credit cards.
- *Minimize Any Other Potential Barriers:* Exempt CDFI Jobs Portals from any other rules that might decrease participation or otherwise limit their charitable and job-creating impact.

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 (via §3(a)(4) of the Securities Act of 1933). These broad exemptions make it simpler for individuals to invest for the public good. In adopting the proposed CDFI Jobs Portal rules for mission investing, the SEC will ensure that its Title III rules reflect its longstanding policy of providing responsible exemptive relief in service of the public interest.

CDFI Jobs Portals: Enhancing Investor and Mission Capital Formation

We 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. The SEC’s rulemaking will be critical in determining the extent to which the legislation achieves its objective of creating jobs while protecting investors.

CDFIs are uniquely well positioned to responsibly channel crowdfunded investment towards the charitable purpose of creating jobs in underserved communities. The proposed CDFI Jobs Portal rules will enhance investor protection while establishing an orderly, efficient marketplace that drives the formation of mission capital at scale.



The CDFI Jobs Portal & Crowdfunding Regulations

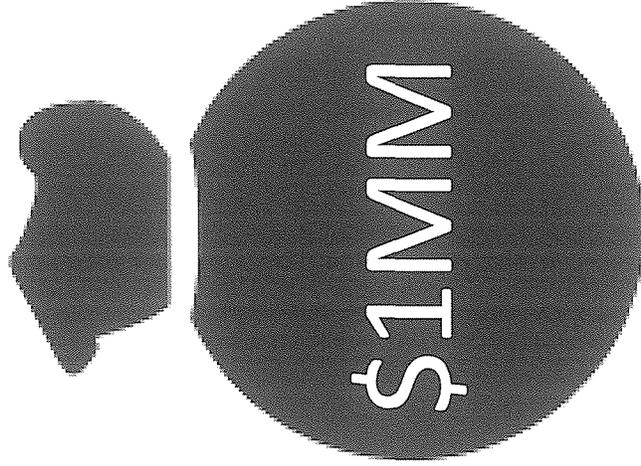
**Protecting investors & creating efficient markets
that facilitate mission **capital formation** through
Title III of the JOBS Act**

Agenda

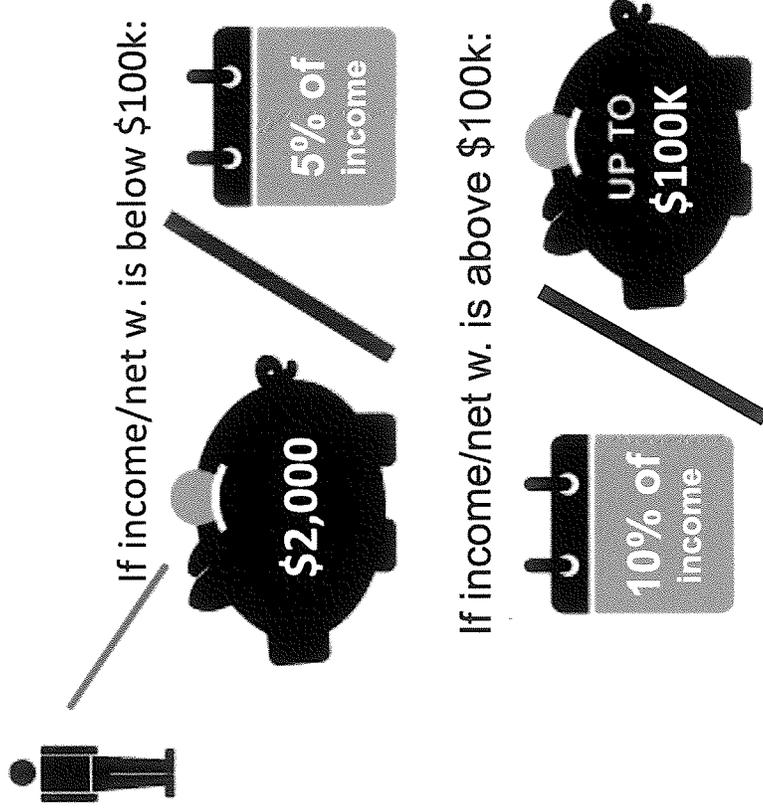
- I. Jobs Act Title III – Securities Crowdfunding
- II. CDFIs: Responsible Capital Formation that Creates Jobs
 - Opportunity to channel crowdfunded capital to underinvested communities & possible barriers
- III. Summary of Proposed Rules
 - Recommendations for alternative set of investor protections
 - Recommendations to facilitate mission capital formation
 - Regulatory Economic Analysis

Title III: Crowdfunding Exemption

1 Limited to \$1MM/12-months



2 Single investor can invest:



Graphics Sourced From: <https://www.bightable.com/infographic/42332>

Goal of Legislation: Create Jobs

Crowdfunding to date is good at raising capital, so-so at creating jobs

Biggest crowdfunded projects:

- Overseas imports: iPhone Doc and Pebble/Nano watches
- Low job creating: video games / apps



TikTok+LunaTik Multi-Touch Watch Kits
by Scott Wilson - MINIMAL

Transform your iPod Nano into the world's coolest multi-touch watches with TikTok + LunaTik by Scott Wilson and MINIMAL.

Chicago, IL

SUCCESSFUL!

6,283%	\$942,578	FUNDED
FUNDED	PLEGGED	DEC 16, 2010



Wasteland 2
by inXile entertainment

Wasteland 2 is a sequel to the amazingly popular 1988 RPG Wasteland and the post-apocalyptic predecessor to the

Newport Beach, CA

SUCCESSFUL!

325%	\$2,933,252	FUNDED
FUNDED	PLEGGED	APR 17, 2012



OUYA: A New Kind of Video Game Console
by OUYA

Cracking open the last closed platform: the TV. A beautiful, affordable console -- built on Android. by the creator of Jambox.

Los Angeles, CA

SUCCESSFUL!

618%	\$5,879,791	8
FUNDED	PLEGGED	DAYS TO GO



Elevation Dock: The Best Dock For iPhone
by Casey Hopkins

Undocking's a breeze and it works with cases. Built at a whole new level of quality with a beautifully minimal design.

Portland, OR

SUCCESSFUL!

1,952%	\$1,464,706	FUNDED
FUNDED	PLEGGED	FEB 11, 2012



Shadowrun Returns
by Harebrained Schemes LLC

Shadowrun Returns brings back one of our most original & cherished game settings as a 2D turn-based RPG for tablets & PC.

Bellevue, WA

SUCCESSFUL!

459%	\$1,836,447	FUNDED
FUNDED	PLEGGED	APR 29, 2012

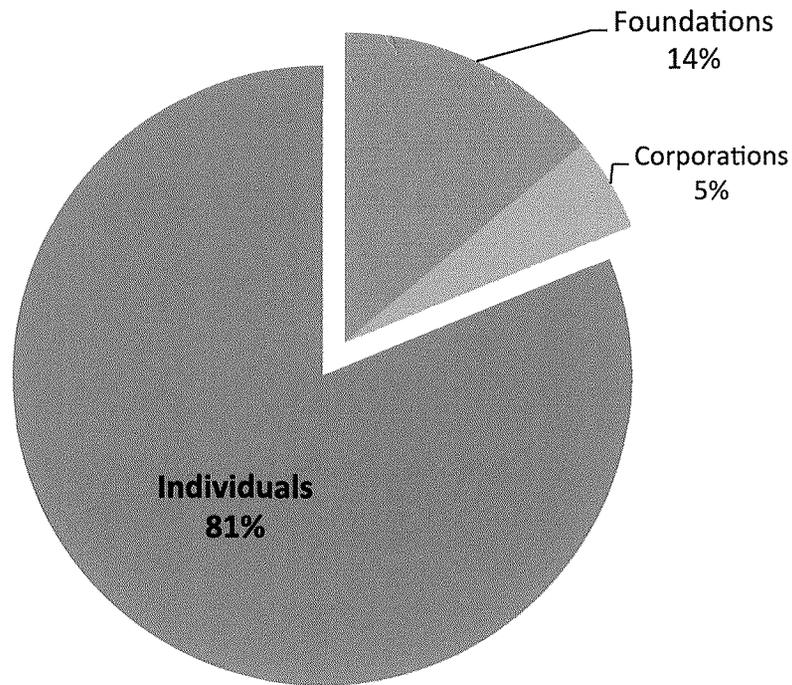
Source: "Kickstarter Most Funded", www.kickstarter.com/discover/most-funded, Accessed 7/17/2012

CDFIs Create Jobs

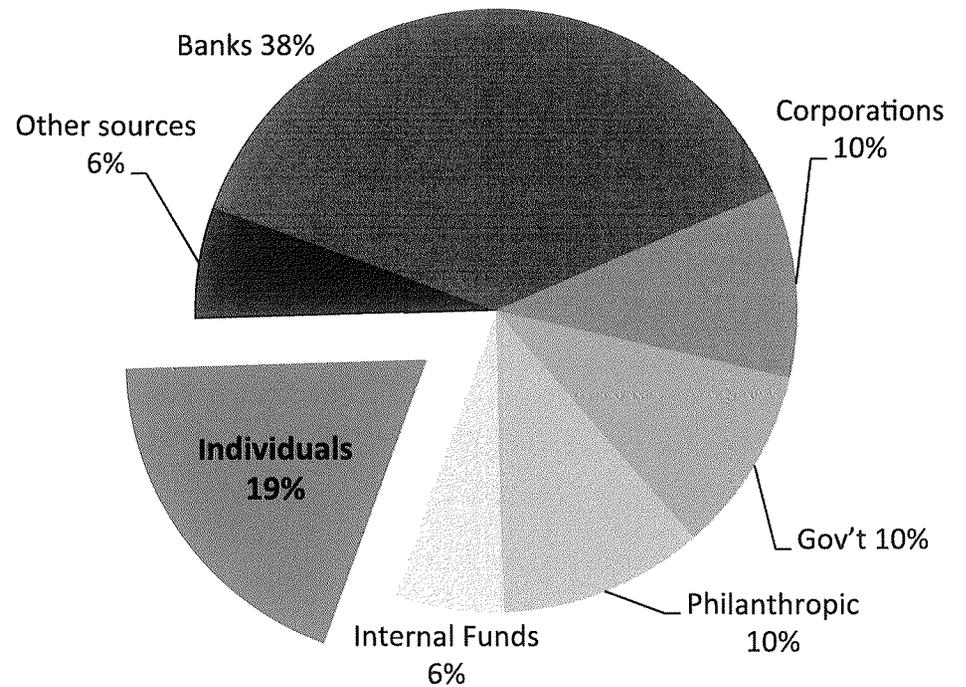
- CDFIs would focus crowdfunded capital on the goal: US Job creation
- CDFIs have capacity & expertise to:
 - Find & fund *job creating* businesses where we need it most
 - Target more funding to low income, underinvested communities
 - Populations with high levels of unemployment
- Over 1,000 CDFIs are active in communities nationwide

Sources of Mission Funding

Charitable Giving Sources



CDFI Capital Sources



Source: First Chart: [2012 Giving USA: The Year in Philanthropy](#), Accessed July 17, 2012, Executive Summary. (2012). Second chart: [The Financial Crisis and CDFIs: A Brief Look at 2007-2009 CDFI Data](#), CDFI Fund.

Challenges for CDFI Participation

Anticipated rules may prevent CDFIs & mission investors from meaningfully participating in crowdfunding for mission impact.

Challenges include:

- Mission investor barriers to entry related to personal disclosure
- Limits on marketing to attract mission investors

Investor Protection Concerns

Securities experts & investor protection advocates urge strong investor protection:

*"A great deal is at stake with the crowdfunding rules, particularly the **potential expansion of fraud** in this area with accompanying harm to small investors. **We urge the Commission to adopt strong investor-protective rules for crowdfunding offerings.** To fall short of this standard creates the risks that **crowdfunding will become a notorious debacle and that many small investors will be harmed.**"*

Secretary of Commonwealth of Massachusetts William F. Galvin

*"The proposals could not only generate **front-page scandals**, but **reduce the very thing they are being promoted to increase: job growth.**"*

Professor John Coates of Harvard Law School

*"**Nothing in the bill requires or even incentivizes issuers to use any capital that may be raised to expand their businesses or create jobs in the U.S.**"*

Commissioner Luis A. Aguilar of the Securities and Exchange Commission

Feedback on Mission-Driven Exemptions

Reducing barriers to entry for mission investors would drive **substantially more job-creation & mission impact**

Broad exemptions without alternative controls **create investor protection risks**: small dollar exemptions create exploitable loopholes

Feedback on Mission-Driven Exemptions

The Commission may be open to creating **safe harbors**, but will need a solution that is:

- **Dependable, financially sound**, and has a proven track record
- Can **facilitate capital formation** at scale w/o introducing loopholes
- Capable of creating a **transparent, orderly, efficient market**
- Strong on **investor protections**
- Strong on **privacy protection**

Proposed Rules to Facilitate Mission Capital Formation

Instead of a broad exemption, create a **targeted alternative set of strong investor protections** appropriate for mission investors through a new type of portal, a **“CDFI Jobs Portal”**

With stronger protections in place, **reduce barriers to entry** for mission-driven capital formation:

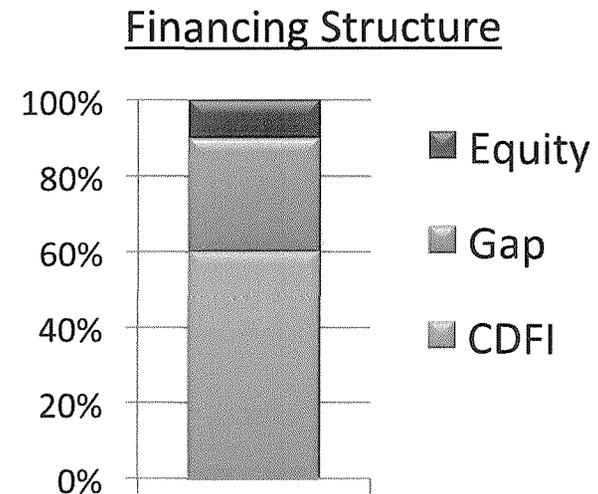
- **Loosen personal disclosure requirements**
- **Clarify marketing limitations**

CDFI Jobs Portal

An alternative investor protection model for mission investors that:

- Requires “skin in the game” from:
 - issuer and
 - a sophisticated CDFI co-investor
- Limits rates of return
- Protects investor privacy
- Ensures safety and soundness of Participating CDFIs

Typically structured as ‘gap financing’



Requirements of CDFI Jobs Portals

CDFI Jobs Portals must be operated by entities that meet **three criteria**.

They must be:

- ✓ **Federally-regulated financial institutions, and**
- ✓ **501(c)3 public charities, and**
- ✓ **Certified CDFIs**

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.

These Include:

- Sophisticated CDFI Co-Investor Requirement
- CDFI Co-Investor Performance Standards Requirement
- Issuer First-Loss Requirement
- Low-Return Debt Requirement
- Privacy Protection Requirement

Senate Co-Author on CDFIs & Crowdfunding

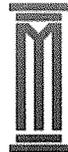
“Suggestions include **ensuring crowdfunding can fill the financing gap for projects** supported by **federally-regulated, 501(c)3 CDFIs**, a clarification to **ensure that CDFIs and issuers can make sure investors understand the mission and charitable aspects of investments**, and **fast treatment from the SEC and FINRA related to registration and membership.**”

-Statement for the Record of Senator Jeff Merkley
Regarding Crowdfunding in Title III of H.R. 3606 July 26,
2012

Milken Institute Crowdfunding Roundtable

Summarizing topline consensus JOBS Act Crowdfunding event:

“Coupling securities crowdfunding with...community development financial institution financing could benefit all involved parties. This partnership would allow crowdfunded businesses to benefit from the expertise of sophisticated investors.”



MILKEN INSTITUTE
CHANGING THE WORLD IN INNOVATIVE WAYS

“Crowdfunding: Promoting the Promise and Minimizing the Peril”,
summarizing July 26th 2012 event. Posted August 2nd, 2012

Investor Protections: Jobs Portal & Standard Portal

Investor Protections	Jobs Portal	Standard Portal
Issuer "skin in the game"	Yes	No
Restricted to low rate of return	Yes	No
CDFI co-investor "skin in the game"	Yes	No
Strict standards & ongoing quality control of CDFI co-investors	Yes	No
Subject to Gramm-Leach-Bliley privacy rules ensuring investor privacy protection	Yes	No
Proven financial strength overseen by Federal regulators	Yes	No
Investor personal data disclosure for maximum aggregate tracking	Yes after \$500	Yes

Permissions: Investor Maximum Aggregate Tracking

Potential Barrier:

Small dollar, mission investors will not have tolerance for personal disclosures (tax returns, SSN)

Proposed rule for CDFI Jobs Portals:

- Portal- Level Tracking Requirement for:
 - Debt instruments offering returns below 5%, and
 - Below \$500 total, with
 - Language indicating below market mission investment
- Aggregate tracking required above \$500

Rationale:

- Investor protection built in by structure:
 - *Small dollar amounts & low returns remove 'get rich quick' temptation*
 - *Federally regulated CDFI portal ensure quality of CDFI sponsors*
 - *CDFI sponsors verify legitimacy of issuers & have "skin in the game"*

Permissions: Clarify Limits on Marketing

Currently:

- No advertising the terms of the offering, except for notices directing investors to portal

Proposed Rule for CDFIs:

- Permit advertising mission elements of the transaction
 - Jobs created, Green impact, Children educated
 - 135c parallel?

Rationale:

- *Mission elements are non-financial, draw interest that is not profit-seeking, and should not be subject to regulation*

Additional Permissions for CDFI Jobs Portals

Permit Categorizing, Searching and Featuring based on non-financial, mission elements of posted offerings

Permit the use of Credit Cards, facilitating ease of investment

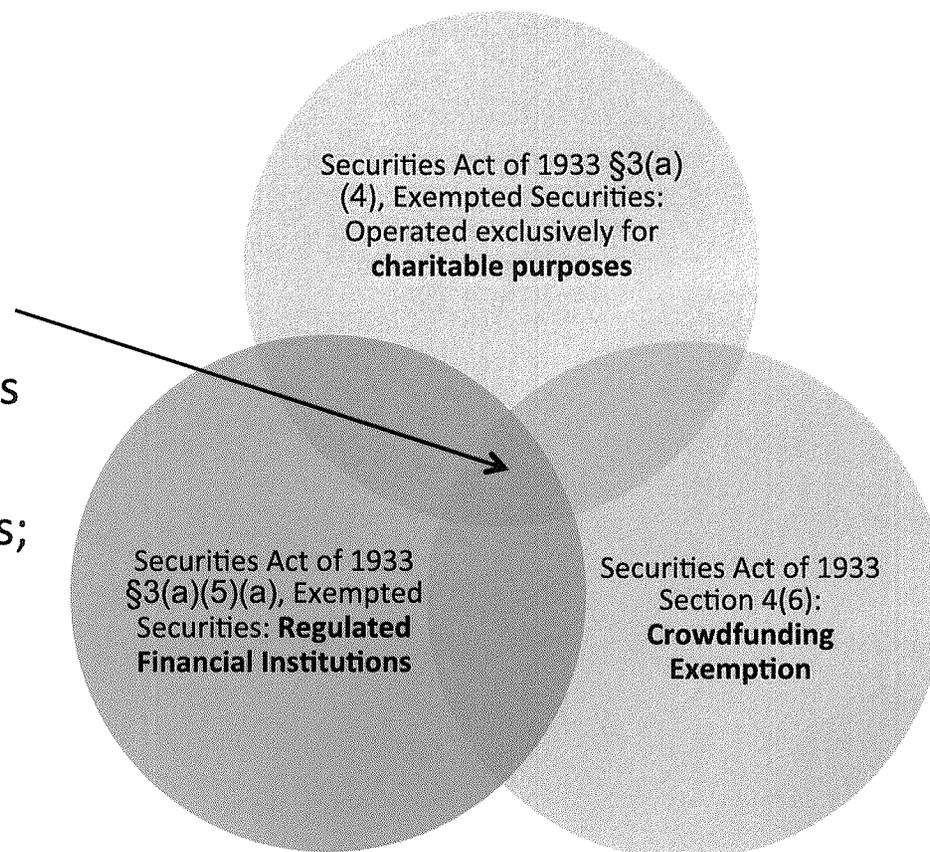
Minimize Any Other Potential Barriers that might decrease participation or otherwise limit their charitable and job-creating impact

Precedence & Strengthening the Crowdfunding Exemption

SEC has a well-established history of providing exemptions for charities and regulated financial institutions

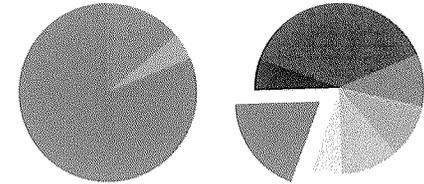
Current proposal may be considered conceptual pairing of crowdfunding exemption with established exemptions in a way that:

- strengthens investor protections;
- allows for mission capital formation;
- creates fair and orderly market



Regulatory Economic Analysis

Baseline: Inefficient market for individual investors



Effect: Many transactions don't come together

Economic impact of proposed rule

CDFI Jobs Portals will secure positive outcomes for:

- Efficiency
- Competition
- Capital formation

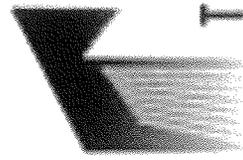
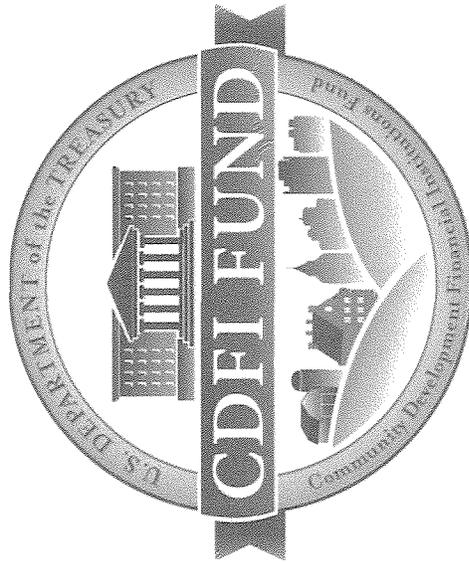
Regulatory Economic Analysis

Significantly diminish capital raising costs for CDFIs and their borrowers, providing broader access to small-dollar mission investors who want to support them

Provide **important community benefits** to underserved communities

Introduce **appropriate but not expensive** investor protection mechanisms relying on **systems that are already in place**

Inter-Agency Hosted Working Group



THE FEDERAL RESERVE
BANK OF RICHMOND

Appendix

SEC Authority within the Act

Portals

- Section 4A(a)(8): Authority to determine **method of tracking with respect to investor limits**
- Section 4A(a)(9): Authority to determine how to ensure **protection of investor privacy**
- Section 4A(a)(12): General authority to establish **rules for investor protection and the public interest**

Issuers

- Section 4A(b)(5): General authority to establish rules for investor protection and the public interest with respect to issuers, including **advertising**

Rulemaking

- Section 4A(c): Broad authority to establish rules for **investor protection**

Importance of consistent disclosure requirements where supplementary protections are not provided

In the absence of supplementary protections, it is important to maintain consistency of disclosure standards.

- Bad actors will flock to less restrictive market
- Low-income investors will only be able to invest in the unrestricted market – exposing highest risk to those who can least afford it

US Income Distribution

% Pop.	Earnings	Max % of income that can be put at risk
7%	Over \$100K	10%
19%	\$50K to \$100K	5%
38%	\$20K to \$50K	5% - 10% (based on universal \$2K limit)
36%	Less than \$20K	10%+ (based on universal \$2K limit)

Source: US Census Bureau 2010

- The portion of the population that can least afford it are able to put the largest percent of their income at risk

Regulatory challenges

- Broadly exempting small-dollar investments from investor disclosures may make it difficult to enforce the statutory limitation on an investor's total crowdfunding investments
- Lower barriers will drive large number of micro-investments (\$5-\$10), driving up enforcement and regulatory costs for only a small portion of total crowdfunded capital formation

***501(c)3 CDFI Federally Regulated Entity**

CDFI Jobs Portal*

