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SECURITIES & EXCHANGE
COMMISSION

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U.S. Securities and Exchange Commission
100 F Street North East
Washington, DC 20549

OFFICE OF INVESTOR
EDUCATION AND ADVOCACY

**RE: SEC Regulatory Initiatives
JOBS Act Title III: Crowdfunding Exemption**

Ladies and Gentlemen:

We are the Crowdfunding Intermediary Regulatory Advocates (“CFIRA”). We wish to thank you for the opportunity to meet with certain Securities and Exchange Commission (“SEC”) representatives on April 20, 2012 to discuss a variety of issues related to the implementation of Title III of the Jumpstart Our Business Startups Act (the “Act”). CFIRA is a coalition comprised of certain of the crowdfunding industry’s leading intermediary platforms and experts actively participating in the crowdfunding industry. Our mission is to facilitate capital formation by creating an equitable, orderly and vibrant crowdfunding market that inspires investor confidence and encourages participation by small businesses and new ventures.

On April 20, 2012, representatives from our organization attended a meeting with certain members of the Corporate Finance Division, Trading and Markets Division and Office of the Compliance Inspection Division of the SEC (the “Staff”) to discuss the new rules and regulations governing crowdfunding to be implemented pursuant to the Act. The meeting was a productive starting point as both the Staff and industry members shared their views of how best to fashion a new regulatory regime tailored to this evolving and rapidly expanding industry.

We respectfully submit the following comments and summarize the views expressed at the meeting with the Staff, along with our comments to certain other provisions of the Act.

We have also included as an attachment to this letter a copy of a letter we are sending to The White House regarding the continued applicability of the general solicitation rules in the context of a Rule 506 private placement.

I. Investor Protection

We believe the success of crowdfunding will be dependent upon recognition of the power, influence and opportunity afforded to entrepreneurs by new media technology and the creation of a comprehensive regulatory framework which protects investors from potential harm. We seek to work with the Staff to develop a system which includes transparency, “crowd-intelligence” and common sense oversight enacted in such a manner that preserves the integrity and scalability of internet-based platforms envisioned by the Act. At the April 20, 2012 meeting, several notable and experienced representatives from intermediary sites, or “portals,” presented a number of infrastructure models and computing and fraud detection systems currently employed in the donation- and rewards-based markets. These models, some of which are discussed in greater detail below, along with models from other business marketplaces and exchanges, *should* be supplemented by additional investor protections, including a portal registry and unique URL’s

for such portals, a background and securities enforcement history check of the officers and directors of the issuer and the portals, required investor education and certain investor due diligence requirements.

a. Infrastructure Models and Computing and Fraud Deterrence and Detection Systems

Section 302(b) of the Act requires crowdfunding intermediaries to implement measures to reduce the risk of fraud. The Act does not mandate the infrastructure that intermediaries must implement in creating their portals. Intermediaries will require a degree of freedom in developing their portals in order to differentiate themselves from one another. That said, we believe the infrastructure utilized by each intermediary should incorporate some type of fraud deterrence and fraud detection system, whether proprietary or licensed through a third party provider. In terms of fraud deterrence, we believe portals should have a video interface whereby each issuer is required to give a short presentation on their business which is capable of being viewed live and saved for later viewing at any time by a potential investor. This will not only help to deter fraud, but it will also enable potential investors to get to know the person with whom he or she is investing. In addition, we believe the SEC should adopt a provision requiring the wiring of the net proceeds from funded offerings to a corporate entity in the US. This will deter fraud from foreign issuers looking to take advantage of the Act's money raising capabilities without being subject to US securities laws.

The SEC should also require intermediaries to build certain fraud detection systems into the functionality of their portal. For example, the SEC should require intermediaries to have a simple "checks and balances" system whereby the portals run a weekly data analysis on a search engine in order to compare the due diligence that was conducted prior to the issuer's posting with any news on the issuer or its officers and directors that has occurred subsequently.

b. Portal Registration

In addition to the protections offered by the portals themselves, we respectfully suggest the Staff consider the creation of a Registered Portal-Check, similar to the Broker-Check system maintained by the Financial Industry Regulatory Authority ("FINRA"). The register will serve to protect both issuers and investors from the risks of unregistered intermediaries and provide greater transparency for all crowdfunding participants. We recommend this system clearly identify the registration status of a funding portal and its management, display any regulatory actions against such portal, and provide a hyperlink to its website. This will provide investors and issuers with an opportunity to easily confirm the registration status of an intermediary site.

c. Due Diligence Requirements With Respect to Issuers

Section 4(a)(5) of the Act requires intermediaries obtain a background and securities enforcement regulatory history check on each officer, director and person holding more than 20 percent of the outstanding equity of every issuer whose securities are offered. However, the Act does not address the extent to which an intermediary must delve into the background of an issuer or how thorough the background check must be. This has the potential to create a barrier to entry restricting opportunities of issuers and intermediaries to adequately protect investors and raise funds. We believe the scale of such background checks should be related to the size of the transaction, while also establishing a minimum requirement that is an effective mechanism against fraud. We believe the SEC should establish a minimum level of diligence an intermediary

must undertake in order to facilitate the sale of an issuer's securities and that such minimum level be below the current requirements for broker-dealers undertaking private placement offerings.

As the Staff considers the scope of the due diligence required by the Act and balances the need to protect investors and the costs of compliance, we emphasize the separate and distinct obligations that should be applicable to funding portals and brokers. Although FINRA has provided its members with guidance on its due diligence obligations in the context of private placements, we note that, unlike broker-dealers, funding portals have a more limited role in the crowdfunding securities transaction, and are subject to greater limitations. Such limitations include a prohibition on providing investment advice or recommendations regarding specific issuers and the amount able to be invested by individual investors. We believe the scope of due diligence required of portals should be limited to conducting a commercially reasonable investigation based upon information publicly available on the SEC and FINRA websites (as well as the website of the self-regulatory organization which will have ultimate oversight of the crowdfunding industry), issuer questionnaires and negative assurances from the issuers' related parties. Again, we believe it most helpful if the Staff provides a safe harbor on what searches and background checks will satisfy this requirement.

II. Securities Offered Through Portals and Financing Mechanics

We believe the Staff should expressly confirm the current language in the Act that any form of equity or debenture security, as well as those convertible or exchangeable for other securities, may be sold pursuant to the Act. A broad spectrum of securities will help to create a more vibrant and useful crowdfunding marketplace. We believe investors can be adequately protected by requiring intermediaries to include a glossary explaining each type of security available for purchase in each of the offerings on its portal.

We accept the Staff's position, which is consistent with historic practice, that a registered investment funding portal which is not duly registered as a broker-dealer should not be permitted to hold funds and that a third-party should be engaged for such purpose.

III. Advertisements and Investment Advice

a. Advertisements

The ability of an issuer and an intermediary to utilize new media technology to generate interest in itself is critical to the success of crowdfunding and can be appropriately balanced with necessary investor protection. Section 302 of the Act expressly prohibits intermediaries from compensating promoters, finders or lead generators for providing the intermediary with the personal identifying information of any potential investor. We would appreciate clarification from the Staff concerning other ways companies can currently generate lists of investors and the myriad of ways to reach them and whether such approaches would conflict with the Staff's concern on general solicitation. The Staff emphasized in its reading of Section 4A of the Act that issuers were prohibited from soliciting investors and that portals may market and advertise to promote the portal itself to attract investors, but may not advertise the terms of any specific offering. We believe clarification should be issued that a portal is allowed to advertise that certain issuers are utilizing their portal without providing any of the terms of a particular offering, should be able to advertise offerings just listed, offerings that were successfully funded (similar to the current broker-dealer practice of utilizing tombstones) and the number of investors in a recently closed offering. Furthermore, issuers should be able to promote their offering through

their own platform as long as all such notices include a link directly to the registered intermediary.

b. Investment Advice

The Staff's interpretation of what constitutes investment advice under the Act is an issue of primary importance to intermediaries. The Act clearly forbids an intermediary from providing investment advice or recommendations whether to invest in a security. However, the Act becomes less transparent when considering, for example, if an intermediary's decision to work with a particular issuer instead of another (whether based upon industry, product, moral or ethical considerations or use of proceeds) constitutes investment advice. CFIRA hopes the Staff will establish bright lines making it clear how an intermediary maintains its independence and avoids being deemed to be giving investment advice.

Intermediaries need the ability to make judgments about issuers within certain parameters, as well as the flexibility to revise those parameters as their own businesses evolve, without having to host every entrepreneur hoping to raise money. Portals must be permitted to be selective in which issuers they permit to sell securities on their interface. We believe such freedom is not only consistent with the intent of Congress, but that it will also augment investor protections as it creates another source through which issuers are vetted prior to raising money from the public.

The need for intermediary discretion without offering investment advice can be satisfied in a few ways. First, require intermediaries to enact and publish pre-established guidelines, terms and conditions setting forth the requirements and processes by which issuers are selected to sell securities through their site. These guidelines may be based on industry, size of company or any other parameters an intermediary chooses to establish. Intermediaries should publish on their websites a disclaimer that its selection or rejection of an issuer does not constitute investment advice. Those guidelines should include the ability to discontinue an issuer's offering based on parameters established in such guidelines. Intermediaries need the ability to modify these parameters in their own business judgment, but such modifications must have been enacted by management consent of such intermediary not less than 30 days prior to such portal offering any investment under such new parameters. Second, provide clear disclosure to, and require express acknowledgement from, investors of the then-existing guidelines.

Although prohibited from giving investment advice, intermediaries will need the flexibility to distinguish themselves from one another in order to compete for issuers and investors. Ways they may seek to accomplish this include by industry, geography and size of company, but will almost certainly include the design and navigability of their site, access by issuers and investors to information about current market conditions and structures of recent deals (whether within a particular industry or in the crowdfunding industry in general) and the look and feel of an issuer presentation (a portal may determine that all issuer presentations must conform to a certain style and may even help with the preparation and editing of such information). We hope the Staff makes it clear that intermediaries will have this flexibility as their business needs evolve and that any such variation will not, in and of itself, constitute advice with respect to a particular investment.

IV. Know Your Crowd and Investor Due Diligence

The Act requires intermediaries to educate investors on the risks associated with crowdfunding securities and ensure that such investors demonstrate an understanding of such risks. Sections 4(a)(3) and 4(a)(4) of the Act require intermediaries to provide certain disclosures relating to risks and other “investor education materials” to investors and ensure that such investors understand them. We agree investors should demonstrate an understanding of and expressly acknowledge, the risks inherent in investing in new ventures and small businesses, as well as the liquidity risks of owning unregistered securities. However, there is ambiguity in the Act which we believe requires clarification from the Staff. For example, the Act does not properly define “investor education materials,” nor does the Act contemplate the frequency with which intermediaries must educate investors or the certainty with which intermediaries must ensure the investors have been educated. The intermediary will control the means by which an investors’ knowledge is checked, but at a minimum, the intermediary should demonstrate that a reasonable person had the opportunity to learn and understand the basics of making an investment of this nature. The intermediary should not be required to educate an investor each time they invest, but every twelve months, an investor should be required to re-enroll in the educational program. The intermediary should be required to update its educational materials as and when appropriate. To ensure an investor understands the educational materials, the investor should affirm via digital signature that he or she understands the educational materials prior to investment. We believe intermediaries should also be required to include a glossary explaining each type of security available for purchase in each of the offerings on the portal. This will put the investor in a more favorable position to make an informed investment decision. It would be most helpful if the Staff provides a safe harbor on what will satisfy these requirements.

Section 302 of the Act establishes investment limits for investors based upon a percentage of such investors’ annual income or net worth. This restriction protects investors from overconcentration in a single issuer and the potential risk of loss associated with new ventures. We believe it is Congress’ intent to protect unaccredited retail investors and we urge the Staff to expressly distinguish between retail and institutional investors and accredited and unaccredited investors in the sale of securities, as it does in other securities transactions. The new regulations should exclude institutional and accredited investors from the definition of “person”, thereby permitting institutions and accredited investors to invest in excess of \$100,000 in any one issuer. Institutional investors have the requisite experience, and both institutional and accredited investors have greater access to resources to conduct comprehensive due diligence and the ability to better manage risk of loss, than an unaccredited retail investor. This key interpretation will provide small businesses and new ventures greater access to capital through a more limited shareholder base. The regulations should also expressly permit crowdfunding funds, provided the sponsors of such funds are responsible for verifying the income or net worth level of their investors in accordance with the requirements set forth in the Act.

In connection with investing in private placement transactions, FINRA currently permits its registered members to confirm a person’s status as an “accredited investor” by completing an investor questionnaire. Current regulations do not require further due diligence to confirm, absent actual knowledge of fraud, a person’s annual income or whether any other “accredited investor” threshold has been properly satisfied. We believe the imposition of any greater due diligence obligation on a crowdfunding intermediary would be impractical and unwarranted. It also seems impractical to require an intermediary to confirm whether an investor has participated in prior

crowdfunding offers on other portals and the extent of any single investor's crowdfunding investments. We respectfully request the Staff clarify that the burden on establishing the accredited status of any investor be to obtain various representations and warranties from the investor, including with respect to any other crowdfunding investments made and that such investor meets the minimum income requirements required by the Act. The Staff should further clarify that an intermediary can only confirm investor compliance with the investment limitations of Section 302 of the Act solely with respect to other crowdfunding investments made through that same intermediary.

V. Crowdfunding and Integration Doctrine

Section 302(a) of the Act permits issuers to sell up to an aggregate of \$1,000,000 of its securities during any 12 month period. Section 4A(g) of the Act states that an issuer is not restricted from raising capital by methods other than crowdfunding, and that businesses may also seek to raise additional capital prior to, concurrently with or subsequent to a crowdfunding offering through a private placement (for example, pursuant to a Rule 506 offering). It therefore suggests that the two offerings are mutually exclusive and should not be subject to the integration doctrine. We respectfully request the implementing rules state clearly that a Rule 506 offering and a crowdfunded offering will never be integrated except under narrow, specifically defined circumstances.

VI. Guidance on Issuer Disclosure

It is a core principal of our regulatory system that investors have equal access to full disclosure of all material information concerning an issuer. The Act requires issuers to provide certain information to investors including, but not limited to, its management structure, business plan, offering amount, capital structure, method of valuing its securities and risk disclosures. To facilitate full disclosure, we respectfully request the Staff provide a form disclosure document for issuers which simplifies the process and provides legal certainty for investors, intermediaries and issuers.

We also note that Section 4A(c) of the Act provides for Section 12(a) liability for material misstatements and omissions. We respectfully suggest that an anti-fraud standard would be more appropriate in this context, since the disclosure requirements under the Act are less than those required in a prospectus filed pursuant to the Securities Act of 1933, as amended.

VII. Crowdfunding Investors and Held of Record Calculation

The Act provides that securities sold in crowdfunding offerings are exempt from the "held of record" calculation in connection with the registration requirements under Section 12(g) of the Securities Exchange Act of 1934, as amended ("Section 12(g)"). Investors who purchase securities in a crowdfunded offering will be restricted from transferring these securities for a period of one year. The Staff has taken the position that the exclusion from the "held of record" calculation attaches to the holder and not the security. Therefore, upon expiration of the one year transfer period and a subsequent transfer by the initial investor, the new shareholder will be included in the "held of record" calculation. Such transfers may trigger the registration requirements of Section 12(g), which will require the issuer to expend valuable time and money to register with the SEC. For small business and startup ventures, this registration requirement could decimate an issuer's working capital and cause irreparable damage to its business and

operating prospects. Such a requirement would also seriously hamper efforts to make crowdfunding a practical, long-term alternative for the investment community. The need for additional capital to meet registration requirements will result in either an issuer borrowing money, thus leveraging its business, or raising additional capital through a subsequent equity offering that will unnecessarily dilute existing stockholders. We respectfully request the Staff either state clearly that the “held of record” calculation attaches to the security and not the holder or extend the exclusion for a period of time well beyond one year.

VIII. Audit Requirements

Under the Act, the extent to which an issuer must disclose its financial statements varies depending on the aggregate amount offered, including any prior offerings in the preceding 12 month period. For crowdfunded offerings with an aggregate offering amount up to \$100,000, the issuer must disclose its most recently filed income tax returns and its financial statements certified by the issuer’s principal executive officer. For offerings that exceed \$100,000 during any 12 month period but are less than \$500,000, the issuer must provide financial statements reviewed by an independent public accountant. If an aggregate offering amount exceeds \$500,000, the issuer must provide audited financial statements. The Act permits the SEC to establish rules amending the \$500,000 threshold requiring audited financial statements.

As the Staff is aware, preparing audited financial statements is a costly, time-consuming process not required of similarly situated private companies raising money under current SEC regulations. We see no reason for a more onerous burden on companies seeking capital through crowdfunding, as this would be a primary obstacle frustrating efforts to raise money pursuant to the Act and a substantial hurdle for the industry as a whole to overcome. We respectfully request the Staff consider the totality of the costs of meeting the foregoing obligations on the issuer, as well as the harmful impact on the nascent crowdfunding industry, and apply the requirement to provide audited financial statements solely to issuers which have been engaged in their current business for more than 12 months and which are seeking to raise at least \$1,000,000. Companies in existence for less than 12 months should further be exempt from providing independently certified financial statements. Such issuers (and perhaps even the intermediaries) should be required to make appropriate disclosure regarding the lack of operating history, the absence of revenue and the unavailability of reviewed financial statements.

Further, we would appreciate clarification from the Staff whether a crowdfunded offering will be considered, for the purposes of the audit provisions, to be “public,” and thus the Generally Accepted Auditing Standards for such an audit will be under the jurisdiction of the PCAOB, or “private” and under the jurisdiction of the ASB (Audit Standards Board). Due to the relative size and nature of crowdfunded offerings, we believe the financial statements should be under the jurisdiction of the ASB, not the PCAOB.

IX. Registration and Self Regulatory Organization

FINRA vs. NFA – Group to discuss.

X. Recommended Timeline

The Act requires the SEC to adopt the final regulatory regime for crowdfunding within a maximum of 270 days of its enactment. We commend the SEC on its prompt action and

consultation with members of our industry. In an effort to continue to build on the constructive relationship that has developed between our organizations and to ensure Congress' timetable is respected, we respectfully propose working together in accordance with the following timetable to ensure this limited rule making period is both productive and comprehensive.

We have identified the following issues in order of priority that we will be analyzing and wish to simultaneous work with you to prepare:

- May - Investor Protection, Due Diligence, Fraud Deterrence and Detection
- June - Advertising and Investment Advice
- July - Registration Process and Self-Regulatory Organization
- August - Disclosure Requirements and Offering Memoranda
- September - Crowdfunding Mechanics
- October - December: Comment Period on Draft Regulations and Adoption
- January 1, 2013 - Crowdfunding Launch Date!!

The members of the Crowdfunding Advisory Group of CFIRA remain available to further discuss the recommendations and concerns expressed in this letter. We look forward to supporting the work of the Staff over the course of the next few months as well as in the future, and to making this program a success for investors, small business and entrepreneurs.

Respectfully submitted,



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CROWDFUNDING INTERMEDIARY REGULATORY ADVOCATES