

William Michael Cunningham

Economist and Social Investing Advisor

March 27, 2015

We understand the SEC is “adopting amendments to Regulation A and other rules and forms to implement Section 401 of the Jumpstart Our Business Startups Act. Section 401 of the JOBS Act added Section 3(b)(2) to the Securities Act of 1933, which directs the Commission to adopt rules exempting from the registration requirements of the Securities Act offerings of up to \$50 million of securities annually. The final rules include issuer eligibility requirements, content and filing requirements for offering statements, and ongoing reporting requirements for issuers in Regulation A offerings.”

I believe I have expertise borne of experience that may be helpful, having authored a book on the JOBS Act titled *The JOBS Act: Crowdfunding for Small Businesses and Startups*. See:

<http://www.amazon.com/JOBS-Act-Crowdfunding-Businesses-Startups/dp/143024755X/>

Further, we remind the SEC that “All men are caught in an inescapable network of mutuality, tied in a single garment of destiny. Whatever affects one directly, affects all indirectly.” This is especially true with respect to the subject matter at issue here.

Summary

Under Title IV of the JOBS Act, the US Securities and Exchange Commission proposed rules to allow small and medium sized companies to raise up to \$50 million via crowdfunding. Some have claimed that the SEC "has taken an important step toward implementing the so-called JOBS Act, making it easier for small and mid-sized businesses to raise capital through small public offerings." Others claim, somewhat breathlessly, that "the SEC is Changing the Rules for Startup Investing." Nonsense. Here is why this move is not as exciting as some claim:

As the Washington Post noted, the SEC "approved rule changes that allow companies to raise up to \$50 million a year, up from a longstanding cap of \$5 million, through what's known as Regulation A offerings. These offerings are exempt "from registering with state financial regulators in every state in which they're prospective shareholders reside." The table below lists the features of this new rule, which becomes effective on May 24, 2015:

| JOBS Act Section | Title IV | | Title III |
|--|--------------|--------------|--------------|
| | Regulation A | | Crowdfunding |
| Maximum you can raise | Tier 1 | \$20,000,000 | \$ 1,000,000 |
| | Tier II | \$50,000,000 | |
| Solicit ANYONE? | | Yes | Yes |
| Crowdfunding online? | | Yes | Yes |
| Can you get money from small, unsophisticated investors? | | Yes | Yes |
| Must register the security offered with the SEC? | | Yes | Form D |
| Register with State Securities regulators? | Tier 1 | Yes | No |
| | Tier II | No | |
| Annual financial reports required? | | Yes | Yes |

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From an operational perspective, this is backwards. Title III, small scale equity crowdfunding, should have come first. This would have allowed the SEC to use experience gained in small scale offerings to set the stage for and improve the larger scale offerings that will be generated from Title IV. (*Note to the SEC - This is probably why Title III came before Title IV in the JOBS Act.*) But, the SEC is looking out for the interests of large, non-small business, non-minority firms. They want them to get control of crowdfunding first. Further, this will limit the ability of women and minority firms to use this Title IV tools, since the firms the SEC has selected to move this initiative forward have been shown to allocate capital services in a racially and gender biased manner. For more, see: <http://youtu.be/ZdKZmKPHIQc>

Given how greedy and unethical most of these firms are, we also expect that these large firms may engage in unscrupulous behavior (see: [SEC v. Citigroup](#), [US v Standards and Poor's](#), and *hundreds* of other cases.) that will then be used as an excuse to slow, if not stop, the implementation of Title III.

Here's the other reason the SEC chose this path: you can hide more lawyer and investment banking fees in a \$50 million dollar offering than you can in a \$1 million dollar offering. This is, of course, contrary to the intent of the law (and the mission of the SEC) since the bulk of the benefit to society will come from those small, less than \$1 million dollar offerings, but this shows who the SEC is really working for.

I'm not sure I'd want to be the first to use this new Title IV facility. State Regulators who have been bypassed are sure to object to the diminution of their authority. This means they will examine each offering issued under these new rules with a microscope. This means further delays in your ability to actually use the law. So, while this rule proposal appears to be a major advance, it is not.

What's really going on is this. The SEC is still seeking to delay the implementation of Title III of the JOBS Act. This is the truly exciting and revolutionary part of the Act. Title III allows anyone to buy equity in very small (micro) companies and startups. They were to have enacted this section of the law by 12/31/2012. (That's right. The SEC is 815 days late in implementing Title III of the JOBS Act (1,085 days late from the April 5, 2012 enactment date). Imagine your boss if you were 1,000 days late with a project at work.)

The facts above are an indication that the Agency has been captured by the large financial institutions it is supposed to regulate. (We don't really expect this to change. Why? Take a look at this.) After all, these large financial firms, the same ones who caused the financial crisis, are the only institutions who would have been left out under Title III.

We suspect the SEC will propose "venture exchanges" as the preferred mechanism for meeting the Agency's obligations under Title III of the JOBS Act (non-accredited small scale equity crowdfunding).

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These will be owned and operated by the NASDAQ and the NYSE. This is prima facie proof of regulatory capture, BTW.

As I discuss elsewhere, the Title IV final rule is the least, and I mean the very least, the SEC can do now. (See: <https://www.udemy.com/how-to-crowdfund> and <https://www.udemy.com/stock-bond-mutualfund-investing>)

We remind the SEC that, under its watch, unethical practices have flourished in capital market institutions, propelling ethical standards of behavior downward. Thus, unethical behavior has become standard in the financial services marketplace.

Conclusion

It has been shown that the SEC does not apply regulatory or enforcement capacities in a competent, fair, racially neutral manner, and we have no reason to believe the Agency will do so here.

The SEC cost the nation \$19.2 trillion, increased the speed with which China will overtake the U.S. in GDP terms, and set the stage for the eventual replacement of the US dollar as global reserve currency. These events tend not to be in the public interest. Given the facts above, we conclude that the Agency is compromised. We note that racial bias is one indicator of a lack of competence.

We look forward to reviewing your continuing efforts to carry out your mission. Please contact me with any questions or comments.

Sincerely,

/William Michael Cunningham/

William Michael Cunningham

Social Investing Adviser for William Michael Cunningham and Creative Investment Research, Inc.

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APPENDIX

Background

William Michael Cunningham is a DC Native. He holds a Master's in Economics and an MBA in Finance, both from the University of Chicago, and is a graduate of Howard University.

Mr. Cunningham manages an investment advisory and research firm, Creative Investment Research, Inc. The firm researches and creates socially responsible investments and provides socially responsible investment advisory services. He is also Managing Partner at National Crowdfunding Services, LLC.

Creative Investment Research, Incorporated is an independent investment research and management firm, founded in 1989. For clients, our services save millions, if not billions: on December 22, 2003, December 22, 2005, and February 6, 2006, we warned the S.E.C. and other regulators that statistical models using our proprietary Fully Adjusted Return® Methodology signaled the probability of system-wide economic and market failure (see below). Clients who heeded our warning adjusted their investment portfolios in a manner that allowed them to escape much of the damage caused by the crisis. The firm was formerly in the pool of Corporate Governance Advisors and Diversity Investing Advisors to CalPERS.

Mr. Cunningham is a Global Member of ISOC, the Internet Society (ISOC), a Public Member of W3C, the World Wide Web Consortium, and an Invited Expert Member in the eGovernment Group of the W3C. On November 16, 1995, he launched one of the first investment advisor websites at www.ari.net/cirm (now www.creativeinvest.com).

Forecasting Track Record

On July 3, 1993, Mr. Cunningham wrote to US Securities and Exchange Commissioner (SEC) Mary Schapiro to notify the Commission about a specific investing scam, the "Nigerian letter scam." A timely warning was not issued to the investing public, members of the public were damaged, and the SEC launched retaliatory regulatory actions against Mr. Cunningham.

He designed the first mortgage security backed by home mortgage loans to low and moderate income persons and originated by minority-owned institutions. (See: *Security Backed Exclusively by Minority Loans*, [The American Banker Newspaper](#). Friday, December 2, 1994.)

Mr. Cunningham [opposed](#) the application, approved by the Federal Reserve Board on September 23, 1998, by Travelers Group Inc., New York, New York, to become a bank holding company. In October 1998, in a petition to the United States Court of Appeals ([Case Number 98-1459](#)) concerning the Travelers Group Inc./Citicorp merger, Mr. Cunningham cited evidence that growing financial market malfeasance greatly exacerbated risks in financial markets, reducing the safety and soundness of large financial institutions.

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From October 1999 to March 2002, Mr. Cunningham was responsible for proxy voting activity for the Board of Pensions of the Evangelical Lutheran Church in America. In 2001, he voted on 1395 issues impacting 401 companies. In 2000, he voted on 1903 issues impacting 422 companies. We managed fund efforts and corporate governance matters related to Talisman Energy and its' operations in the Sudan. We researched the issue, contacting various groups involved in the process. For the fund, our efforts also included researching fund policies and procedures. Our collaborative, risk controlled strategy helped lead the firm out of the Sudan. On February 1, 2000, Mr. Cunningham wrote to the office of U.S. Senator Samuel Brownback (R-KS) urging him to encourage pension funds to divest from the Sudan.

On June 15, 2000, Mr. Cunningham testified before the Financial Services Subcommittee on Capital Markets, Insurance and Government Sponsored Enterprises (GSE's) of the U.S. House of Representatives and suggested that GSEs Fannie Mae and Freddie Mac be subject to a Social Audit. A social audit is an examination of the performance of an enterprise relative to certain social return objectives. It includes a review of ethical practices. Had the GSE's been subject to this audit, certain flaws in their operation, including ethical shortcomings, would have been revealed earlier, in a better market in which to make corrections.

In 2001, Mr. Cunningham participated in the first wide scale home mortgage loan modification project. The Minneapolis-based effort helped 50 families victimized by predatory lending practices. [See: Property Flipping Remediation Yields Investment-grade Security.](#)

On December 22, 2003, he warned US regulators that statistical models he created using the proprietary Fully Adjusted Return® Methodology signaled the probability of system-wide economic and market failure. [See Page 6.](#)

In 2005, Mr. Cunningham served as an expert witness in a case that sought to hold Credit Suisse First Boston, Fairbanks/SPS, Moody's and Standard and Poor's, US National Bank Association, and other parties legally responsible for supporting and facilitating fraudulent subprime lending market activities. Had this single case been successful, we believe the credit crisis would have been less severe.

On December 22, 2005, he issued a strongly worded warning that system-wide economic and market failure was a growing possibility in a meeting at the SEC with Ms. Elaine M. Hartmann of the Division of Market Regulation.

On February 6, 2006, he again warned regulators that statistical models created using the proprietary Fully Adjusted Return® Methodology confirmed that system-wide economic and market failure was a growing possibility. He stated that: Without meaningful reform there is a small, but significant and growing, risk that our (market) system will simply cease functioning. This is, of course, exactly what happened. [See pages 2 and 8.](#)

On June 18, 2009, he testified before the House Ways and Means Select Revenue Measures Subcommittee at a joint hearing with the Subcommittee on Domestic Monetary Policy and Technology of the Financial Services Committee: Testimony on the New Markets Tax Credit Program. He suggested

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ways to improve the program. See:

http://www.novoco.com/new_markets/resource_files/advocacy/cunningham_testimony_061809.pdf

On Wednesday, January 13, 2010 and Monday, June 14, 2010, Mr. Cunningham wrote to Mr. Phil Angelides, Chairman, Financial Crisis Inquiry Commission, to submit testimony and comments to the Commission. In addition, he noted that he was “disappointed that FCIC has not sought out or recognized a broader set of opinions and viewpoints and are further disappointed by FCIC’s lack of ethnic diversity at both the Board and Staff level.”

On July 19, 2010, Mr. Cunningham testified on behalf of the public at the Joint Interagency Public CRA hearings: “The Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation and the Office of the Comptroller of the Currency jointly held public hearings on modernizing the regulations that implement the Community Reinvestment Act (CRA).” See:

http://www.fdic.gov/CRAhearings/Individual_Presentations.pdf

On August 13, 2012, Mr. Cunningham filed a "Friend of the Court" brief in United States Securities & Exchange Commission vs. Citigroup Global Markets Inc. (Second Circuit Court of Appeals Case Number 11-5227). The case concerned the rejection, by a Federal Judge, of a settlement agreed to by the United States Securities & Exchange Commission (SEC) and Citigroup Global Markets Inc. (Citigroup), the latter accused of securities fraud. <http://www.prlog.org/11948760-william-michael-cunningham-files-revised-brief-in-sec-vs-citigroup-2nd-cir-ct-of-ap.html>

On December 9, 2013, Mr. Cunningham filed a "[Friend of the Court](#)" brief in the United States District Court, Central District of California in a case concerning an action that the U.S. Department of Justice, acting on behalf of the United States of America (Plaintiff), brought against McGraw-Hill Companies, Inc., and Standard & Poor’s Financial Services LLC, et. al., (Defendants) under 12 U.S.C. § 1833a; 18 U.S.C. §§ 1341, 1343 & 1344. My comments led to a significant change in enforcement strategy, including the first ever, albeit temporary, rating firm suspension.

On February 3, 2015, I commented on an effort by Apple Computer to utilize women and minority-owned brokerage firms: <http://www.usatoday.com/story/tech/2015/02/03/apple-debt-offering-minority-firms-jesse-jackson-diversity-silicon-valley/22805673/>

Mr. Cunningham writes commentary on small business topics for the Washington Post. For more background information, please see:

[Global Market Turmoil Graphic](#) and [Financial Crisis Calendar Graphic](#), Creative Investment Research, Inc., December, 2008 and November, 2009.

Equity Crowdfunding: <https://youtu.be/1802x3V-EhA>

Black Economic Forecast: https://youtu.be/rlr_DomOais, https://youtu.be/E_AgImRM_Wk

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