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March 22, 2014

Elizabeth M. Murphy
Secretary
U.S. Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

SUBJECT: File Number S7-11-13 – Release 33-9497, Additional Comments Related to BDCs

Dear Ms. Murphy,

This is an additional comment letter submitted on behalf of Commonwealth Fund LLC (CF),¹ a community economic development organization dedicated to the establishment of a new type of Business Development Company (BDC) focused on economic development at a regional rather than national level.

The SEC has requested input from interested parties to assist in answering questions that arose during preparation of the proposed Title IV rules with the proposed Tier 1 & Tier 2 offerings (hereinafter Regulation A or Reg A and Regulation A+ or Reg A+ and collectively Reg A/A+). One of the areas addressed pertained to BDCs and whether they should be allowed to use Reg A/A+.

We have provided the Commission a separate comment letter dated March 21, 2014 that responded to the specific questions put forth by the Commission on that subject. However, we felt that there were a number of related issues, primarily pertaining to BDCs, that were not addressed by the Commission in its request for comments, that nonetheless have relevance.

Our comments and recommendations for this letter are enumerated below, followed by an analysis as to why we are making such recommendations, and what benefit we believe they will provide.

GENERAL RECOMMENDATION

In our previous comment letter, we pointed out that BDCs are an excellent vehicle for addressing the capital formation requirements of a broad spectrum of Main Street small businesses and that allowing them to use Reg A/A+ to obtain the funding to carry out that objective is very much in sync with the broader goals Congress had in mind with the passage of the JOBS Act.

Regardless of whether the Commission authorizes BDCs to use Reg A/A+, we believe regional BDCs are a very appropriate vehicle for local economic development and should be actively used. Our organization intends to do so with local partners across the country. Using Reg A/A+ would make that goal much easier to achieve, for many of the same reasons that individual companies use those exempt offerings to bridge the gap between being small privately funded companies and becoming fully fledged reporting public companies.

Nonetheless, if necessary we will use the standard N-2 registration process and subsequent public reporting requirements, because we think that BDCs are important to aiding capital formation for small businesses at the local level. It would be far easier to establish and launch such efforts if we and others

¹ <http://www.commonwealthfund.us>

could use Reg A/A+ to get those BDCs up and running and ultimately grow them into fully reporting companies.

However, simply approving the use of Reg A/A+ for BDCs does not provide all the tools needed by regional BDCs attempting to serve the needs of local communities and their small businesses. There are other issues related to BDCs that we feel should be addressed by the Commission to further enhance their ability to carry out that function. Below we make a number of observations and recommendations that are intended to better enable local BDCs to serve their communities and to facilitate that effort in conjunction with other local stakeholders.

SPECIFIC RECOMMENDATIONS

1. Determination of the value of the BDC's portfolio assets resulting in the BDC's net asset value (NAV) should include the option to use other metrics than solely financial, including social and environmental metrics.
2. Candidate BDC portfolio clients (BDC client) should be allowed to solicit investors to invest in the BDC using crowdfunding promotional tools and techniques with the provision that such investments would inure to the benefit of the BDC client, without the BDC client being considered an un-registered finder/broker/dealer.
3. Regional BDCs should themselves be considered "eligible portfolio company" for purposes of investment in and the establishment by other BDCs.
4. The effective date of a Reg A/A+ offering by a regional BDC should be within a certain time frame after filing the Form 1-A with the SEC, provided that the SEC has not objected to the application due to a material issue prior to that date, or alternatively a BDC can obtain an accelerated approval provided that it follows a particular regional BDC Form 1-A template.
5. Community banks should be exempt from SEC Regulation R and be allowed to serve as investment bankers (for primary offerings), transfer agents and listing services (for secondary trades) for these regional BDCs and their client companies.
6. When a regional BDC uses Reg A (Tier 1) for an offering up to \$5 million, then the BDC should be able to use the same investor qualifications found in Tier 2 offerings, primarily in the state where the BDC is headquartered and any state with borders immediately contiguous to that state, thereby obviating the need for further state qualification of the offering.

ANALYSIS OF THE RECOMMENDATIONS

1. Determination of Net Asset Value and the Valuation of Portfolio Investments

When Congress enacted the legislation enabling BDCs, it required them to disclose to the public their net asset value (NAV) on a quarterly basis. Congress did not provide for a specific way for a BDC to determine its NAV, but rather required management, the board of directors and advisors to the BDC to come up with a rational basis for determining the value of the company's assets and therefore the company as a whole, and to disclose that rationale to the public. Congress further authorized BDCs to use a different book value for their assets from their cost, based in part on the premise that an asset in a public company may be worth more than what it cost the BDC to acquire.

That leads to the question of why a regional BDC should be allowed to include social and environmental metrics when determining the value of its portfolio assets and of the BDC itself. The answer lies in the local investment movement and the concept of socially responsible investing (SRI).² Each incorporates additional metrics to determine the worth and importance of investments.

We find that local investors are often investing with motivations and goals that are not restricted to purely financial returns. This phenomenon is well chronicled in a number of books and articles from authors

² http://en.wikipedia.org/wiki/Socially_Responsible_Investment

such as Michael Shuman³ and Marjorie Kelly.⁴ They and others report that a substantial portion of local investors make an investment decision based on concerns for the economic health of their communities just as much, if not more so, than for the financial returns they can expect.

Likewise, the broader SRI movement (often also called impact investing), which includes the local investment movement but goes beyond it to the national and international levels, is focused on what is often called a double (financial and social) or triple (financial, social and environmental) bottom line.

The federal government, via the U.S. Economic Development Administration, has recognized the importance of this movement and funded the development of a web-based tool for evaluating companies, projects and communities along these additional dimensions.⁵ Thus we see a widespread and growing interest in the business community for evaluating and valuing companies beyond purely financial terms and it is appropriate for regional BDCs to incorporate these additional metrics.

How That Could Work

Currently financial markets value companies based on some evaluation of that company's financial bottom line. However, one of the ramifications of that valuation metric is the downward pressure that puts on payroll costs of the company, resulting in the growing criticism of low wages and the economic disparity that produces.

When looked at from a local community perspective, the lower the wages paid to local workers, the less money is injected into the local economy. And conversely, the more those employees are compensated, the more dollars are available for circulation within the community.

Thus most communities would prefer that local employees be paid higher wages, even though that would yield smaller financial bottom lines for the companies paying those wages. If a BDC were allowed to value a company based on how much it injects money into the local economy via increased salaries, taxes and the like, the more that valuation would align with the way that the community and its local investors would value those companies.

And a solid case can be made that the community would value a local company more if it was a good environmental steward and not only did not pollute the local environment, but helped to make it cleaner and more healthy. Such efforts could cost the company money and therefore reduce its financial bottom lines, but would produce yields that the community would value equally if not more so than its net profits. Thus we see an additional reason to allow regional BDCs to factor in these other variables in making a determination as to the value of their underlying assets and thus the value of the BDC as a whole.

2. Targeted Investments

One of the ways a regional BDC could operate is to provide a means for its investors to express their preference on how they would like to see the BDC use their money. That could include the BDC inviting investors to identify broad categories of investment preferences, such as minority-owned businesses (including race, gender, economically disadvantaged and other identifiable groups), green technology companies (such as renewable energy, clean tech and other green categories), geographic areas and so on. The BDC need not be obligated, but could make a "best effort" commitment to honor those preferences.

³ <http://www.cuttingedgecapital.com/team/michael-shuman> and his book *Local Dollars, Local Sense: How to Move Your Money from Wall Street to Main Street and Achieve Real Prosperity*

http://www.chelseagreen.com/bookstore/item/local_dollars_local_sense

⁴ <http://www.cuttingedgecapital.com/marjorie-kelly> and her book *Owning Our Future: The Emerging Ownership Revolution* <http://www.marjoriekelly.com/books/owning-our-future>

⁵ See Triple Bottom Line Tool <http://tbltool.org/> funded by the U.S. Economic Development Administration

This concept can be extended to include preferences for investments in specific companies. This could be a way to leverage the crowdfunding movement and its tools and techniques to the direct benefit of individual companies, but in the context of an investment through a BDC.

How That Could Work

A BDC, upon evaluating a prospective investment in a small local business, could elect to provide a targeted investment in that particular company. The BDC could allow the company to reach out to its supporters and ask them to invest in the BDC with the intention of having the BDC incorporate their investment into the funds the BDC will allocate to that particular company. Those target companies could use the same tools and techniques that they would use in promoting their own crowdfunding offering (social media, their corporate website, email campaigns, etc.) but potential investors would be guided to a page on the BDC's website where they could elect to make their targeted investment via the BDC.

This way the company receives the funds it might otherwise get via its own crowdfunded offering, but its investors would have the safety and benefit of owning shares in the publicly traded BDC while getting funding to that company nonetheless. The company has the added benefit of having to deal with only one investor, the BDC, but also gets the benefit of the mentoring and monitoring that the BDC is mandated to offer its client companies, thereby enhancing the company's survivability.

On the BDC side, this technique could have the additional benefit of providing positive feedback from the community that the targeted company has support, a fact that could be especially important for early stage companies without a track record, customer base or any history to evaluate.

Existing companies are easier to assess, but the BDC can still benefit from that same feedback providing reinforcement for its decision to invest. In both cases, for a startup or mature company, the BDC does not need to use this process to raise all the money it might provide the company, but could use it to make a go/no go decision on the investment in a fashion similar to crowdfunding portals that establish a threshold for a particular crowdfunding offering before releasing those funds to the company.

"Finders" Exemption

This brings us to the particular recommendation we made concerning companies making use of such targeted investment with a BDC. We assume that the BDC should be allowed to provide for its investors to express their preference for the use of their funds. However, that could prove problematic with respect to individual companies using that technique to drive investments to themselves.

Given that the target company would be soliciting investors for another entity (the BDC) and that such solicitation could provide a direct economic benefit back to the target company (i.e., the BDC goes forward with the investment in the company), those target companies might be considered unlicensed "finders" or broker/dealers unless the Commission exempts them from being considered so in this context. This is the basis for our recommendation to exempt those companies from unlicensed finder status.

3. Allowing BDCs to Invest In and Launch Regional BDCs

We recommend that the kinds of regional BDCs contemplated herein should themselves be considered as "eligible portfolio companies" as defined in the 1940 Act such that other BDCs can invest in and help to establish regional BDCs.

How That Could Work

We can envision a larger regional BDC funded by a Regulation A+ offering and/or a standard N-2 filing, focused on somewhat larger investments in its local region, nonetheless wishing to help nurture investments in micro-enterprises as contemplated in our earlier comment letter dated March 21, 2014. Given that working with such companies may entail a very different approach than with somewhat larger companies, the initial BDC might want to help another group (a non-profit incubator, for example) to set

up a separate BDC just for such micro-enterprise investments. If the larger BDC can consider the smaller BDC as an eligible portfolio company, it can help launch and fund that smaller BDC as it would any other portfolio investment, thereby giving the smaller BDC sufficient resources to establish its operations and raise its own funding (probably via a Tier 1 Reg A offering).

Likewise our organization, Commonwealth Fund LLC, intends to help establish regional BDCs throughout the country, normally in partnership with local parties interested in funding their local businesses. We in turn would like to establish a national BDC that helps communities to establish such regional BDCs and thus we would like to consider those regional BDCs as eligible portfolio companies for our BDC. Our BDC could help to provide a template structure to those local partners in a fashion not dissimilar to what a franchisor does for its franchisees, thereby both accelerating the establishment of such regional BDCs and ensuring their greater success by adopting a proven model. Thus, when we help to set up such a local BDC, we have a direct and ongoing interest in the Commission allowing these regional BDCs to use Reg A/A+ to fund their local operations.

4. Effective Date

In an effort to further reduce the regulatory burden and costs associated with a regional BDC's effort to raise funding from its local supporters, we recommend that the SEC consider either providing for an automatic approval of the Form 1-A Regulation A/A+ offering filing done by or on behalf of a regional BDC, or an expedited approval process if those BDCs follow a prescribed application process as defined below. Should the Commission entertain an automatic approval, we would encourage that it be tied to a time interval, such as by the thirtieth day following the filing, if prior to that date the SEC has not provided a rejection of application for a material cause.

Non-material elements such as the omission of certain names or facts or the need to clarify certain information shall not constitute material cause that would delay the approval, even though the SEC may respond to the applicant with a request for such data or clarification. To delay the automatic approval, we would suggest that the SEC have to declare in writing, before that date, what material fact, omission, clarification or other response is needed in order to approve the application. Otherwise the application shall be considered to have had automatic approval by the thirtieth day, thereby ensuring timely approval for local BDC needing to get on with supporting its local businesses.

If automatic approval by a date certain is deemed unworkable, then an expedited approval process tied to a pre-defined application specifically designed for these regional BDCs would be a good alternative. It may not provide for a predictable date, but a strong likelihood of approval would have similar benefits for the BDC, and coupled with the Reg A "testing of the waters" option, would allow a prospective BDC to focus on its business objectives without waiting to commence its business planning until it has been officially approved to carry out its funding objectives.

Commonwealth Fund would be glad to work with the Commission to develop one or more templates of a Form 1-A designed to go specifically with a regional BDC seeking approval for a Reg A or Reg A+ offering, with the understanding that if an applicant used such a template, the SEC would have confidence that an appropriate application has been filed that conforms to the needs of both the SEC and the applicant regional BDC. We intend to standardize our BDC websites, offering documents and all other aspects of establishing and running such a BDC, and that template business plan would be provided to the Commission as well as shared with our partners and others interested in launching their own independent regional BDCs.

5. The Role of Community Banks With Our BDCs And An Exemption from SEC Regulation R

There is one industry player that has not had much involvement in the small business capital formation space but represents a significant, untapped resource — the nation’s community banks,⁶ thrifts and credit unions (hereinafter collectively “community banks”). They have historically provided a substantial portion of the credit needed by our country’s small businesses, but have not addressed their capital needs.

Community banks, probably better than any other financial institution, have a finger on the economic pulse of America’s small businesses and are better equipped to work with them on both their credit and capital formation needs than just about any other group, including broker dealers. In fact, their loan review committees already use a comprehensive set of tools for evaluating the economic health of a small business and those tools can just as easily be applied to capital formation as they are to credit evaluation.

However, unlike big banks that work with their large corporate clients on all aspects of their financial needs, community banks have focused solely on the credit needs of their small business clients. Yet given the current economic and regulatory climate, community banks need to expand their product base, and investment banking and related activities could be an excellent fit.

Our organization (Commonwealth Fund) has developed a program to take advantage of those community banking resources and financial skills, wherein we intend to have community banks actively involved in the vetting and evaluation of our BDC candidate portfolio companies. Having a community bank perform the financial vetting of our prospective investments would be viewed as highly desirable by all stakeholders. And doing so would not require those banks to step out of their comfort zone or require any additional regulatory compliance.

However, we would also like them to participate in the capital formation (i.e., investment banking) component of our BDC activities, but here we encounter an obstacle. If any bank, large or small, wants to lead an investment banking activity, then SEC Regulation R requires that they also become registered broker/dealers under FINRA. We have had extensive dealings with individual community banks, community bankers and community banking associations, and even though they have expressed strong interest in this idea, they find the Reg R requirement too high a hurdle.

Community banks already are one of the most heavily regulated sectors of our economy. A common complaint is that their regulatory environment has worsened since 2008 even though big banks, not they, were the cause of the financial crisis. The prospects of taking on a greater regulatory burden by having to become a FINRA registered broker/dealer is out of the question for most community banks, which cannot afford the additional costs of time and money in compliance. So even though community banks would be one of the best sources for investment banking services to small businesses, few will take that step on their own. This leads us to ask why they are required to be licensed broker/dealers in the first place.

Fraud and bad actor behavior is almost non-existent in the community banking industry. The same cannot be said for the big banks or the broker/dealer industry, where the regulatory watchdog role is appropriate and very much needed. Community banks are a different matter. For example, we were able to find only two instances of banking fraud and embezzlement in the state of Ohio over the last 25 years. A brief exploration into the BD world will quickly uncover a substantial number of disciplinary actions that dwarf that number. Thus we repeat our question – why are banks required to be licensed BDs? What is the public being protected from that is not already covered under banking charters and their regulatory environment?

⁶ The Federal Deposit Insurance Corporation (FDIC) has until very recently defined a community bank as one with assets of \$1 billion or less. In its comprehensive 2012 study on community banks, FDIC slightly modified that definition, but the old definition is adequate for our purposes. We also are including thrifts and credit unions that serve small businesses in our definition.

It is our understanding that banks, along with thrifts and credit unions, have long been allowed to participate in all manner of securities transactions, but it wasn't until the passage of Reg R in the late 1990s that those institutions were no longer allowed to take on a primary role (rather than a support role to a licensed BD) without also having to be a licensed BD as well as a chartered banking institution. That may make sense for the big banks, whose behavior warrants that regulatory supervision and can afford it, but it does not make sense that community banks should also bear that burden.

Therefore we would like to propose to the Commission that community banks (including thrifts and credit unions with less than \$1 billion in assets) be exempt from compliance with Regulation R and be allowed to conduct all manner of investment banking, be a transfer agent and trustee, and facilitate secondary trading of the securities offered by our regional BDCs (if not all small company offerings). That exemption should also cover any wholly owned subsidiaries of those community banks, along with any jointly owned subsidiaries (whether in partnership with other banks or non-bank entities) in which the bank is the controlling party.

That way the bank can partner with other organizations that have small business capital formation expertise (angel groups, VCs, incubators, SBDCs, economic development groups, etc.), as long as the bank maintains control, responsibility and liability for the operation. We believe that in providing that exemption, the SEC will unlock a critical resource for our nation that could have a dramatic and positive impact on small business capital formation, while at the same time engaging a partner in the critical role of investor protection that would be hard to beat. Community bankers personify the embodiment of fiduciary duty, and should they stand at the center of the small business capital formation space, the SEC, the investor public and all other stakeholders should have high confidence that their interests are being protected.

6. Investor Qualification

Much has been said about the industry's desire to have federal preemption over Blue Sky laws with respect to Regulation A, Tier 1 offerings. While we understand why some have wanted such Reg A preemption in order to carry out nationwide offerings on a cost-effective basis, we are interested in enabling local funding for our regional BDCs and do not propose that Reg A, Tier 1 be preemptive on a national basis.

We do, however, strongly recommend that with respect to our regional BDCs, it would be very helpful if the BDC can use the same investor qualification for a Tier 1 offering as the Commission has proposed for a standard Tier 2 offering, i.e., the "qualified purchaser" definition, in the state where the BDC is located and making the offering. Given that a BDC will have more investor protections than regular companies seeking Reg A/A+ approval (per our previous Reg A/A+ - BDC comment letter dated March 21, 2014 and per the additional involvement of community banks that we propose), we feel that investors will already be adequately protected.

Should the Commission agree with that same state investor qualification, we would also like to propose that the concept be extended to adjacent states that are immediately contiguous to the primary offering state.

For example, our organization is headquartered in Youngstown, Ohio, in an area called the Mahoning Valley. We sit right on the eastern border of Ohio and a portion of western Pennsylvania is considered part of that valley and region. Were we to set up a regional small BDC focused on micro-enterprises, we would have to reject investment from our Pennsylvania neighbors just down the street, who would have an interest in our mutual local businesses equal to ours, if we did not file a Blue Sky filing with both states. There are a large number of similar border-straddling communities throughout the country. Thus using the investor qualification with respect to both states would be beneficial and would remove the corresponding burdens that would otherwise be present.

SUMMARY

We feel that regional BDCs are a very important tool in the small business capital formation space and strongly encourage the SEC to aid such organizations as much as possible. That would include not only allowing them to use Reg A/A+ offerings as we spelled out in our earlier comment letter, but also by helping to put in place as many of the above recommendations as the Commission can implement. Doing so will, in our estimation, help to ensure optimum usage of these regional BDCS for the benefit of all stakeholders and greatly enhance the ability of communities and local groups to serve the needs of a larger percentage of their local small businesses than crowdfunding alone could provide.

We thank the Commission for its efforts in this direction and in considering our recommendations. We look forward to working with the Staff and to making regional BDC investing a success for investors, small businesses, entrepreneurs and the communities they support.

If you have any questions regarding this letter, please contact Michael Sauvante at (650) 641-1246 or at [REDACTED]

Respectfully submitted,



Michael Sauvante, Executive Director