

August 30, 2012

Marcia E. Asquith
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1506

RE: FINRA Regulatory Notice 12-34: Request for Comment on Proposed Regulation of Crowdfunding Activities

Ladies and Gentlemen,

We are the Crowdfunding Intermediary Regulatory Advocates (“CFIRA”). CFIRA is a coalition of over one hundred of the crowdfunding industry’s leading platforms and experts comprised of portal CEOs, broker/dealers, industry service providers, and attorneys. Our mission is to facilitate capital formation by creating an equitable, orderly and vibrant crowdfunding market.

We appreciate the opportunity to respond to FINRA’s request for comment on the proposed regulation of crowdfunding activities. We respectfully submit the following comments in regards to potential rules concerning supervision, advertising, fraud and manipulation and crowdfunding activities of existing broker dealers, in addition to other comments on certain other provisions of the Act.

I. Investor Protection

We believe the success of crowdfunding will be dependent upon the creation of a comprehensive regulatory framework that enables small businesses and startups to access the capital they need while protecting investors from potential harm. We seek to work with FINRA 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. As early as April 2012, 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. Specifically, we recommend including a portal registry, a background and securities enforcement history check of the officers and directors of the issuer and the portals, 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 platforms. 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. FINRA should also require intermediaries to build certain fraud detection systems into the functionality of their portal.

b. Portal Check

We respectfully recommend FINRA consider the creation of a “Registered Portal-Check” to list all intermediaries registered to conduct crowdfunding similar to the Broker-Check system currently maintained by 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 type and status of an intermediary 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. 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 FINRA should establish a minimum level of diligence an intermediary must undertake in order to facilitate the sale of an issuer’s securities but that the minimum level be well below the current requirements for broker-dealers undertaking private placement offerings.

As FINRA 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 crowdfunding. Although FINRA has provided its members with guidance on its due diligence obligations in the context of private placements, we note that, unlike traditional private placement’s, crowdfunding capital raises are much smaller, often micro-raises as small as \$10,000. As such, we believe the scope of due diligence required in crowdfunding should be limited to conducting a commercially reasonable investigation based upon information obtained from third-party service providers (checking criminal, civil, securities regulatory, and credit history of the issuer and of directors, officers and 20%+ shareholders), checking the issuing entities good-standing status in their state of formation, and relying on issuer disclosures on their PPM and any questionnaires and negative assurances from the issuers’ related parties. We believe there should be a safe harbor on what searches and background checks will satisfy this requirement.

II. 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 FINRA concerning other ways companies can currently generate lists of investors and the myriad ways to reach them and whether such approaches would conflict with the Commission's concern on general solicitation. We believe clarification should be issued regarding a portal being allowed to advertise that certain issuers are utilizing their portal without providing 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 as long as all such notices include a link directly to the registered intermediary.

b. Investment Advice

The interpretation of what constitutes investment advice under the Act is an issue of primary importance to intermediaries. The Act clearly forbids "Fundng Portals" from providing investment advice or recommendations whether to invest in a security. However, the Act becomes less transparent when considering, for example, if a Portal'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.

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 platforms. We believe such freedom is not only consistent with the intent of Congress, but that it will also enhance investor protections as it creates another source through which issuers are vetted prior to raising money from the public.

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, for example, include by industry, geography and size of company. We hope FINRA 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.

III. Know Your Crowd and Investor Due Diligence

The Act requires crowdfunding 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 be required to go through a mandatory educational process before they begin investing on the platform, demonstrating an understanding of and expressly acknowledging, 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 FINRA. For example, the Act does not define "investor education materials," nor does the Act contemplate the frequency with which intermediaries must educate investors. The intermediary will control the means by which an investor's 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. The intermediary should be required to update its educational materials when appropriate. To ensure an investor understands the educational materials, the investor should affirm 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 will be helpful if FINRA provides clarification and a safe harbor on what will satisfy educational requirements.

Section 302 of the Act establishes investment limits for investors based upon a percentage of such investors' annual income or net worth. We believe it is Congress' intent to protect unaccredited retail investors and we urge FINRA to expressly distinguish between accredited and unaccredited investors in the sale of securities, as it does in other securities transactions. The new regulations should exclude accredited investors from the definition of "person", thereby permitting accredited investors to invest in excess of \$100,000 in a 365 day period and/or in any one issuer. Such 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 investor.

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 FINRA clarify that the burden on establishing the 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.

IV. Application of Existing Rules to Crowdfunding Activities of Broker-Dealers

The JOBS Act does not limit the FINRA rules applicable to registered broker-dealers engaging in crowdfunding activities. However, we urge FINRA to relax such rules to address a broker-dealer's crowdfunding activities because otherwise, crowdfunding would likely not be economical in such micro-funding raises (which may be as small as \$10,000) given the high degree of due diligence required under existing FINRA rules.

V. Recommended Timeline

We hope FINRA continues to actively engage with the SEC so that FINRA is in a position to issue its rules concurrently with the issuance of the SEC's rules. In an effort to continue building on the constructive relationship that has developed between our organizations, we respectfully offer our expertise to you whenever requested to help ensure the rule making period is as viable as it is comprehensive.

The members of CFIRA remain available to further discuss the recommendations and opinions expressed in this letter. We look forward to supporting the work of FINRA during this rulemaking period, as well as in the future, and to making this program a success for investors, small businesses and entrepreneurs.

VI. Conclusion and Summary

We believe that Crowdfunding, implemented with an eye towards lower cost structures for issuers, will unlock job creation opportunities for issuers and enable unaccredited investors to round out their personal portfolios with crowdfunding offerings.

We believe that FINRA can help the SEC strike an even balance between risk and regulation and create a vibrant industry through a strong regulatory framework, reasonable allowances for portals and issuers to communicate the offerings, and reasonable investor education requirements, including the following:

- Requiring fraud prevention and detection mechanisms on crowdfunding portals.
- Creating a registered Portal-Check to list all intermediaries registered to conduct Crowdfunding similar to the Broker-Check system currently maintained by FINRA.
- Specifying that the scope of due diligence requirements be reasonable and requisite with the size of Crowdfunding rounds, including:
 - A commercially reasonable investigation based upon information obtained from third-party service providers,
 - A check of the issuer's good-standing in their state of formation, and
 - A reliance on issuer disclosures on their PPM and any questionnaires and negative assurances from the issuers' related parties.
- Allowing portals and issuers to openly advertise certain aspects of the offerings including new listings, successfully funded offerings, and the number of investors in a recently closed offering.
- Allowing portals to be selective in curating offerings for their constituents whether by industry, location, size, mission, products, and the reputation and history of the investors and officers behind the issuance. Curation rights and selectivity should not be constituted as investing advice.
- Specifying reasonable investor education requirements.
- Clarifying that investment limits are related to unaccredited investors and that accredited investors are not subject to the same protections.
- Clarifying that the burden on establishing the compliance status of any investor be through self-representations and self-warranty, including with respect to any other Crowdfunding investments made and that such investor meets the minimum income requirements required by the Act.
- Enabling registered broker dealers to address their Crowdfunding activities with the same rules as portal operators.

Please do not hesitate to contact Freeman White (freeman@launcht.com) or Vince Molinari (vmolinari@gatetechnologies.com) regarding the statements and positions outlined in this letter.

Respectfully submitted,

CROWDFUNDING INTERMEDIARY REGULATORY ADVOCATES

By: /s/ Freeman White
/s/ Scott Purcell
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