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VIA EMAIL

MAY 29, 2020

Vanessa Countryman
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: File No. S7–05–20 Facilitating Capital Formation and Expanding Investment Opportunities by Improving Access to Capital in Private Markets

Dear Madam Secretary,

Crowdfund Capital Advisors ("CCA") is a fintech policy and regulatory consulting and advisory services firm. It's principals co-authored the "Crowdfunding Exemption Framework" which became the basis of Title III of the U.S. JOBS Act to legalize equity and lending-based crowdfunding. They were called to testify in front of five US House and Senate Committee hearings related to crowdfunding. They attended the JOBS Act bill signing ceremony at the White House and were honored to work alongside the Commission on shaping the final Rules for Regulation Crowdfunding.

CCA created the industry's first crowdfunding database. CCLEAR, as it is known, collects, cleans, aggregates and reports on trends in the industry. Because we have data on all the offerings, including daily transactional information, we can provide real-time transparency and insights that can inform policy decisions on early-stage investing. The days of making claims about legislators, regulators, investors and the media not knowing what is happening in this part of the private capital markets ended in 2016 when Regulation Crowdfunding went into effect.

CCA serves certain governments and multi-lateral organizations including Inter-American Development Bank, the World Bank, governments of Singapore, Mexico, Chile, Malaysia, Israel, Taiwan and the UAE, professional investors, crowdfunding professionals and the entrepreneurial community. CCA co-authored the World Bank's research report "*Crowdfunding's Potential for the Developing World*" as well as the MIF report "*Creating a Crowdfunding Ecosystem in Chile.*"

We commend the Commission for the time, energy and effort they are putting forth to assist small businesses. We are writing to express our support for the proposed release 33-10763 in its entirety. In particular, we are supportive of:

- Increasing the maximum raise from $1.07 million to $5 million;
- Changing the non-accredited investors limits based on the greater of an income or net worth standard;
- Allowing for the use of crowdfunding vehicles;
- Increasing the reviewed financial threshold to $500,000 raises and audits to $5 million for initial offerings.

Regulation Crowdfunding Framework – Brings Data, Transparency and Analysis to a Segment of the Private Markets

There is universal agreement that accurate and timely data can help drive decisions. Unlike other parts of the private capital markets where data is either nonexistent or difficult to source, the structure for Regulation Crowdfunding requires issuers to make public, information about their business and financial history. This is unique in the private markets today and provides greater transparency than is offered to accredited investors in the pre-IPO private markets today for well-known tech stocks. These required disclosures include:

- the name, legal status, physical address and website address of the issuer;
- the names of the directors and officers (and any persons occupying a similar status or performing a similar function), and each person holding more than 20 percent of the shares of the issuer;
- a description of the business of the issuer and the anticipated business plan of the issuer;
- a description of the financial condition of the issuer;
- a description of the stated purpose and intended use of the proceeds of the offering sought by the issuer with respect to the target offering amount;
- the target offering amount, the deadline to reach the target offering amount and regular updates about the progress of the issuer in meeting the target offering amount;
- the price to the public of the securities or the method for determining the price; and
- a description of the ownership and capital structure of the issuer.

In addition, the regulation requires that these private issuers file annual reports that includes updated information on an issuer's financial wellbeing. This data is already aggregated and tracked centrally by CCA and has been made available to the SEC on a periodic basis.

With all this information and data, we began tracking and analyzing this formerly opaque market. We now have data to not just analyze companies to benefit investors but to analyze industry data to inform policy changes like this one. For issuers raising money via Regulation Crowdfunding, we know who is raising money, how they are using it, what industries they are in, how their valuations compare, where they are located, have they created jobs, how their operations have changed over time, and much more.

With over 2,500 companies filing and disclosing we can tell the following about Regulation Crowdfunding offerings in comparison to other parts of the private capital markets:

- They are accompanied by more robust accounting and financial practices;
- Their disclosures make information, including third party research, more readily available;
- Their securities are more easily and reliably valued;
- Investors in these securities have transparency into the rights of all shares offered;
- Emerging Alternative Trading Systems will offer a transparent and efficient method to liquidate shares of common stock;
    - This will lead to reduced liquidity risks and trading costs;
- There is now the ability to benchmark, such as against the S&P 500; and
    - Actual net performance shows yields better than the public markets and does not benefit one class of investor over another.

Regulation Crowdfunding Performance – Slow Adoption, Steady Growth, Poised for Expansion

The data is clear. Regulation Crowdfunding has spurred innovation, provided access to capital and stimulated economic activity without causing any systemic problems. Since its inception[1]:

- Over $373,000,000 has been invested into
- Over 1,500 companies in
- Over 90 industries (based on Morningstar classifications)
- That has supported over 96,000 jobs
- And has delivered over $600,000,000 in economic activity to local economies in
- 49 States (plus Puerto Rico and Washington, DC) by
- Over 525,000 investors (both retail and accredited)
- 60% of issuers are successful in raising capital and anecdotal evidence indicates that women and minority business owners have benefited from this method to access capital markets
- **With zero instances of fraud**

The above data comes from CCLEAR which as mentioned earlier, aggregates data from all the offerings on all the platforms that are registered with the SEC and overseen by FINRA. We use this data to publish dashboards on our website. We also use this data to provide analysis. We are pleased that our data analysis has been referenced in several publications by the Commission and has been used by other financial regulators in other countries.

Could Crowdfunding be a Counter-Cyclical Access to Capital Opportunity?

During the current global pandemic, we have noticed an increased trend in the number of new offerings. This could be attributed to general year of year growth however, if you search the offerings for the words, 'covid, coronavirus, covid-19 or pandemic' you will see several offerings reference this. Many of these businesses are not able to access capital from traditional sources like banks and are turning to their customers, friends, followers, etc to help provide them with critical capital.

Increasing the cap to $5 million will provide a balanced way for more issuers to raise funds from investors they are closest to, with prescriptive disclosures that inform/protect investors. Increasing the maximum raise provides immediate and long term impact:

- It will allow more companies to raise the capital they need to survive today.
- Post-pandemic, increasing the offering cap to $5 million will allow more mid-sized businesses that need in excess of $1 million to leverage this exemption for funds. It also enables an emerging tech company outside of Silicon Valley or New York City to raise a full seed round to hire employees and build products.

Regulation Crowdfunding is an Economic Engine that Safely Engages Retail Investors

In the 4 years since Regulation Crowdfunding went into effect, there have been no media stories about fraud. Rather there has been unspoken coverage of the benefit these locally supported businesses have provided. For instance, when digging into the data we see that Regulation Crowdfunding has:

[1] Regulation Crowdfunding just finished its fourth complete fiscal year. We summarized the four years of data in this report, *Regulation Crowdfunding Finishes its Fourth Fiscal Year with Some Impressive Results – Industry Poised for Significant Growth*

- **Supported over 96,000 jobs**. According to Paychex[2], for every one direct employee a small business has, they support 7 indirect employees in the form of 1099 vendors, suppliers, repair staff, etc. Data filed on Form C shows that over 12,000 direct jobs have been supported, if this is multiplied by 7 (per the Paychex study) that equals 84,000 indirect employees. 12,000 direct + 84,000 indirect jobs = 96,000 jobs supported.
- **Pumped over $600 million into local economies around the country**. The majority of these businesses are over 1 year old and are not sole proprietorships that pass through their earnings. They use the majority of their revenue to pay expenses to third parties that allow them to both operate and grow. Hence, it is safe to assume that the majority of the $600 million in revenue generated has been pumped back into local economies paying for local products and services. It has been documented[3] that this capital circulates around local economies and provides a lifeline that is necessary for communities to function.
- **Safely engages both retail and accredited investors.** Based on interviews we conducted with the companies raising funds, over 80% of the money has come from people with a first or second degree association to either the company or the entrepreneur. This proves that customers, fans, friends and followers have an appetite for investing into community businesses they use and entrepreneurs they trust. Based on interviews we conducted with platforms hosting these offerings, on average 80% of the investors are retail (unaccredited) and 20% are accredited. Platforms also state that 80% of the capital comes from the accredited investors. This proves a few things:
    - Retail investors aren't taking the majority of the risk in these offerings,
    - Accredited investors, who have the ability to invest wherever they wish, are not just keeping their capital in the public markets or with Venture Capital/Private Equity/Hedge Funds but diversifying and allocating a small percent into local businesses, and
    - You don't have to be "rich" to want to be an investor in a business that you believe in.

Valuations Appear Roughly Similar to Typical Angel/VC Seed Rounds

While the public markets benefit from analysts that offer buy/sell/hold decisions, these types of analysts/analysis can now be more effective thanks to the availability of this data. Because Regulation Crowdfunding delivers transparency, some of the readily available data points to support investor decisions include valuation, revenues and net income.

Because companies must disclose how a valuation was determined and potential investors can discuss this on the forum part of an offering page, it provides investors a means to determine whether they agree with that valuation or not (prior to investing). It cannot be stressed enough how this transparency is unique investor protection in the private capital markets.

Valuations for Regulation Crowdfunding offerings vary depending on age of the firm, revenues, industry and more. Here are some key valuation findings:

- Firms that were successful with Regulation Crowdfunding had an average valuation of $10.7 million.
- Firms that were less than 3 years old had a valuation of $7.9 million,
- Startups with no revenue had an average valuation of $10.1 million and
- Firms with revenues over $1 million had average valuations of $19 million.

[2] https://www.prnewswire.com/news-releases/new-paychex-data-shows-independent-contractor-growth-outpaces-employee-hiring-in-small-businesses-300775712.html

[3] Amy Cortese wrote the book Locavesting (https://www.locavesting.com/the-book/) that details how investments into local community businesses circulates that capital multiple times within that community.

Based on data from angel and Venture Capital investors, the average (pre-covid) Seed pre-money valuation was $7.5 - $15 million and, the average Series A valuation was $20 - $25 million so there is opportunity for investors to invest early, with a little capital, with potential appreciation in follow on rounds.

Issuers Perform Better Year Over Year

In order to understand how issuers are performing, we have 3 components within the Regulation Crowdfunding framework that can bring clarity:

- First, in an initial offering, issuers are required to file disclosures that look at the change in their financial wellbeing between the most recent fiscal year and the prior fiscal year.
- Second, firms that are successful with a raise must file an annual report that discloses the changes in their financial wellbeing year over year since their raise. And
- Third, there have been almost 150 companies that have leveraged Regulation Crowdfunding for follow on rounds. Each time an offering is made a valuation is disclosed.

Based on this we look into the data on Form C, Form C-AR and valuations over time to discover:

- Average revenues increased 34%, demonstrating that these company are growing. This growth rate may be higher than most SMEs without access to capital. Based on interviews with the firms this may be due to availability of growth capital. They may also benefit from community-based investors actively using the firm's services and becoming brand ambassadors in their communities.
- Average net income decreased 62%, proving these companies are spending considerably more year over year, reinvesting capital and profits back into local economies and providing the reason for why Regulation Crowdfunding delivers community-wide benefits.
- Average valuations increased 66% - Demonstrating that Regulation Crowdfunding investments can provide attractive yields to early investors in this segment of the private capital market.

Put simply, the data shows on average these companies are performing exceedingly well and it will be of interest to continue tracking the data during and following the Covid19 recession to assess if capital from crowdfunding is either cyclical or counter-cyclical.

There Has Been ZERO Fraud and No Reported Failure

According to a 2019 report by the Commission on the 3 year history of Regulation Crowdfunding there has been zero instances of fraud. As stated, "In particular, a search of publicly available information in the Commission's litigation releases has not identified civil complaints or administrative proceedings filed against Regulation Crowdfunding issuers or intermediaries.[4]"

There has also been no systematic perversion of retail or accredited investors. This is probably a result of several interconnected ecosystem components either built into the regulations or by the crowdfunding platforms' processes:

1. Regulated platforms that onboard issuers, perform background checks and disqualify bad actors.
2. A disclosure regime that would force bad actors to create "worthy" false documents that would take more time and effort than using a less structured way to commit fraud.
3. Online vetting by the crowd that allows them to pick apart an offering online with the ability to withdraw commitments prior to closing.

[4] https://www.sec.gov/files/regulation-crowdfunding-2019_0.pdf, p.42

4. Online forum whereby the crowd gets to ask questions to the issuer and the issuer must respond with credible answers.

The average campaign has 422 investors, most of whom are likely in the same community as the business raising money. These investors have all reviewed the exact same information, on the exact same platform, in the exact same format. This real-time transparency offers significant investor protection and reduces opportunities for fraud. With this disclosure, if any systemic issues developed, those investors could seek legal recourse as appropriate.

Investors Tend to Have a First or Second Degree Relationship to the Issuer

In interviews conducted with both issuers and portals, it was discovered that the majority of the investors in these offerings had a first or second degree relationship to the issuer and/or industry knowledge about the company's product, services, IP or technology. Any of these creates a degree of trust that doesn't exist between investors and public companies, which is why public companies must file detailed disclosures. This trust allows for strong relationships to build between a Regulation Crowdfunding company and its investors. It also deters fraud as fraud would destroy a business if it was uncovered.

People who have this type of relationship, knowledge or interest should be allowed to invest in businesses they know and entrepreneurs they believe in. It is similar to how many investors choose public stocks today. We should continue to encourage investing in SMEs that includes robust disclosures like those in Regulation Crowdfunding.

Investor Risk is Lower Because of Investment Caps

Unlike the public markets, where there are no restrictions on how much an investor may risk, within the framework for Regulation Crowdfunding there are caps. For example, with the proposed amendment, a retail investor that makes $75,000/year and has $150,000 in savings can only invest $3,750 per year[5].

Because these offerings are open to retail as well as accredited investors, we now have the ability for the democratization of both investment opportunities and capital such that the majority of investors in the US now have greater access to new opportunities with prudent guardrails. Based on the crowdfunding data from the last 4 years, the average investment is currently approximately $715. This is an investment quantum that does not appear to raise immediate concerns of undue concentration risk for most individuals with the appetite and ability to make early stage investments. This average investment size could also suggest a low propensity for a loss of this investment to be a catastrophic loss of the individual's entire investible capital.

The Exemption is Very Prescriptive, and Information is Centralized - Which Benefits Investors

The policy and regulation for crowdfunding includes a very prescriptive and balanced way for both issuers to raise capital as well as investor to risk capital. This includes a series of disclosures that is more fulsome than other exemptions. These disclosures provide investors with detail about a company's operations, financial history and governance.

In addition, this exemption provided under Regulation Crowdfunding allows prospective investors to ask questions directly to the issuers. Their answers help inform not only their own investment decision, but because these

[5] According to the current Regulation Crowdfunding rules, limits on how much each investor may invest over the course of a 12-month period in the aggregate across all crowdfunding offerings depend on the investor's annual income or net worth. If either the investor's annual income or net worth is less than $107,000, the limit equals the greater of $2,200 or five percent of the lesser of the annual income or net worth. If both the investor's annual income and net worth are at least $107,000, then the limit equals ten percent of the lesser of the annual income or net worth, up to a maximum of $107,000. With the proposed rule changes, the maximum a retail investor in the example above would be able to invest would be $7,500 also capping the amount an investor can lose. These types of investor caps do not exist in the public markets.

questions and answers are available for all to see, all prospective investors benefit. Any material misstatements to these questions by the issuer can be used against them should legal action be required.

Finally, the system doesn't benefit one class of investors over another in an offering as they are all presented the same information which is available from one central location the online investment platform, as opposed other exemptions where individual offering memorandums can be amended over time from one group of investors to another.

This Change to Fundraising Limits Does Not Change Any Material Misstatement, Misrepresentation or Purposeful Neglect Clauses

The disclosures required by Regulation Crowdfunding make it easier to identify issuer or executive misconduct. Put simply, the Regulation Crowdfunding disclosure framework improves issuer conduct and accountability. Scaling regulation to ease bureaucracy does nothing to change any material misstatement in disclosures. No matter the size of the company, false statements in offering disclosures may give rise to strict liability, which incentivizes companies to ensure their accuracy.

Because there are robust disclosures, any material misstatements, misrepresentations or purposely neglected information can be used against the issuer. In cases involving misleading statements or omissions, a class period generally starts when a company makes an untrue statement of material fact about the company or fails to disclose a material fact necessary to render other statements not misleading. Thus, the negative legal and financial burden for company misstatements is not reduced. In addition, potential investor lawsuits serve not only to provide recourse for injured investors, but also strongly discourage other issuer misconduct.

Escrow and Minimum Target Thresholds that Protect Crowdfunding Investors are Not in Other Exemptions

In order for a Regulation Crowdfunding issuer to receive its capital commitments it must hit a minimum funding target by a specified deadline. This does two things; a) it forces an issuer to hit and exceed a target or a campaign fails and b) it triggers the return of capital that has been committed and sits in an escrow account. These types of safety triggers are similar to provisions/protections used by traditional early stage investors (i.e. Setting a size for the round, stating a minimum amount for the "first close" and "final close" and using escrow to hold funds until the funding targets are met. Crowdfunding offers similar ways to mitigate risk for all investors.

If we look at the crowdfunding data, 40% of Regulation Crowdfunding issuers failed to hit their minimum funding target prior to their deadline. These issuers only had 2.8% of all the capital committed since Regulation Crowdfunding launched. That capital was returned to the investors – meaning no investor losses for unsuccessful campaigns. This type of investor protection does not exist elsewhere in the capital markets.

Increasing the Cap will Reduce the Cost of Capital

In a research study[6] our firm conducted, we discovered that the average campaign spends 5.29% of their proceeds putting an offering page together, creating company disclosures, filming the campaign video, hiring a marketing firm, lawyer and accountant. So, the average firm that is currently raising around $260,000 would be spending $13,754 to put their campaign together. However, many of these costs may be fixed (i.e. an accountant may charge $5,000 for an audit of a startup with limited history and financials or a company that uses LawCloud for their disclosures, may pay a fixed amount of $1,500 for an offering in excess of $50,000). Increasing the maximum that can be raised from $1 million to $5 million will spread these costs out and decrease the fees as a percent of the

[6] https://venturebeat.com/2018/08/26/how-much-does-a-regulation-crowdfunding-campaign-actually-cost/

raise. This not only benefits issuers but investors as their capital investment goes into growing/scaling a company as opposed to paying offering fees.

Increasing the cap to $5m would also enable larger, mid-sized firms, (that may be more stable and lower risk) to use crowdfunding for expansion capital and job creation. This adds more diversity of risk levels to the investment landscape which is an investor protection.

The Realtime Actionable Data Available Today Brings More Transparency, Visibility and Accountability

Regulation Crowdfunding has delivered data and standardized datasets on private companies that never existed before and that have now become norm in the industry. This allows for more transparency into the private capital markets than has ever existed. Because of this data we can provide insight into how the industry is growing, where capital is flowing based on demographics, how economic activity is positively impacted (based on analysis of annual reports that are required by law), how jobs are promoted, and more. All of this reduces fraud, and decreases cost and risk to investors

A significant benefit of this set of data/disclosures is that for the first time, we have a way to compare and determine valuations and the financial health/power of SMEs. As mentioned earlier, because data about a company's financials and valuation are public, analysis on share price/valuation can be published to benefit investors. Now we can benchmark these assets, risk profiles and returns taking out the guess and judgment generally required for any benchmarking or indexing making it easier to compare investments.

Regulation Needs to Scale to the Size of a Business

We believe that regulation must scale to fit the size of a business and that an issuer that is not the same in terms of revenue (i.e. millions vs hundreds of millions), complexity (i.e. local operations vs national or international), tax practices (domestic vs international), etc should not be held to the same standards as a public company. This would be overly burdensome for them without providing additional benefit. In essence, the larger the corporation the more complex. The smaller the less complex. We feel that Regulation Crowdfunding does a fair job in terms of trying to balance the needs of the business with the needs of the investor. We believe that the changes proposed by the Commission work in line with goal that regulation needs to scale to the size of the business.

Implement, Review and Increase the Regulation Crowdfunding Cap to $20 Million

The system is working. Making these proposed changes will help thousands of smaller enterprises access capital in a rational way while delivering robust transparency and investor protections. We would suggest an additional review period of 12 to 24 months post effective date of this change, to analyze the data, verify that the system continues to function efficiently, understand how capital is flowing, confirm fraud is nonmaterial and then increase the cap from $5 million to $20 million. This will fill the void that Tier 1 of Reg A has created, as issuers find the challenge of state registration to be overly burdensome.

The broad use of Regulation Crowdfunding across the United States proves that this exemption can democratize access to capital, and that you don't have to be in Silicon Valley in order to raise funds. It also proves that Regulation Crowdfunding works across many industries and can be an important growth tool for companies looking for capital.

Regulation Crowdfunding is also a jobs engine and we have a clear reason why the government should be heavily promoting it – particularly given the current economic crisis facing us.

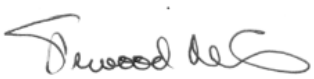
Regulation Crowdfunding is here to stay. And it will continue to play an important role in the funding lifecycle between an entrepreneur's personal access to capital and VC/Private Equity funds. It won't replace those important sources of capital but rather act as a gating mechanism so that VCs/Private Equity and Asset Managers have a better understanding as to where they should be deploying capital. This might make sense anyway since one of the ways VCs diligence potential investments is through the lenses of customers. If a firm's cap table is made up of a roster of customers that believe in the firm (and are willing to put their money where their mouth is), well then you've answered one of the biggest question VCs have prior to investing (i.e. Do people really buy the product/use the service/believe in the founder)?

It is inaccurate and unfair for any individual or organization to say that there is no transparency in this segment of the private capital markets. There is more data and more prescriptive disclosures than probably anywhere else in the private markets with the exception of Regulation A.

People and organizations should not hide behind 80 year old arguments that "investors are unaware" in private transactions. If they do, they clearly haven't read the Regulation Crowdfunding regulations or analyzed tens of thousands of pages of disclosures or carefully analyzed the data. If they did, they would realize that due to this piece of legislation investors now have access to more data and information to make an informed decision than they ever did before. Given this alone, the cap should be increased so larger companies that wish to raise significant amount of capital can do it while providing investors more detail about their offering and business operations than they might via other exempt offerings.

Based on the significant decrease in the number of public offerings due to process complexity and compliance costs, it is critical that the SEC create exemptions that facilitate capital formation while protecting investors. We commend the Commission Concept Release on Harmonization of Securities Offerings in its efforts to accomplish this. With the current economic crisis in front of the United States due to the Coronavirus, making the private markets more efficient is even more important than ever before.

As always, we stand ready to answer any questions you may have.



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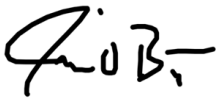

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