The Commonwealth of Massachusetts
Secretary of the Commonwealth
State House, Boston, Massachusetts 02133

William Francis Galvin
Secretary of the Commonwealth

February 3, 2014

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

Re: Comments on the Securities and Exchange Commission Crowdfunding Rule Proposal under Title III of the JOBS Act
Release Nos. 33-9470; 34-7074; File No. S7-09-13

Dear Secretary Murphy:

The Office of the Secretary of the Commonwealth, Massachusetts Securities Division appreciates this opportunity to comment on the Securities and Exchange Commission's (the "SEC" or the "Commission") proposed regulations for crowdfunding under Title III of the Jumpstart Our Business Startups Act ("JOBS Act").

Introduction

The crowdfunding exemption breaks new ground in several ways. The new exemption relies on the "wisdom of crowds" to help determine the value and genuineness of securities offerings conducted online. It creates a new class of non-broker financial intermediaries that will be subject to far less regulation and oversight than traditional broker-dealer firms. The new exemption also will impose ongoing financial reporting obligations on the companies that raise money through crowdfunding. Because crowdfunding offerings will involve significant numbers of small and unsophisticated purchasers, it is crucial that the SEC's crowdfunding rules protect vulnerable investors.

It is vitally important for the SEC to set up a regulatory framework that will protect small investors, small issuers (who will often have limited sophistication and experience), and the financial markets. We urge the SEC to put into place disclosure and regulatory standards that will provide transparency with respect to companies that use the crowdfunding exemption and the intermediaries that sell the offerings. The Commission must also adopt reporting standards that will permit investors to buy and sell these securities in the aftermarket based on sufficient and accurate information.

Issuer-Related Comments:

Remove the Safe Harbor for "Insignificant Deviations"

The proposing release includes a safe harbor that allows an issuer to have the benefit of the exemption even if it does not comply with all of its conditions, so long as the failure to comply is "insignificant with respect to the offering as a whole" and the issuer made a "good faith and reasonable attempt" to comply.

This safe harbor will be detrimental to state enforcement efforts. We foresee that issuers of some unregistered offerings will assert that their transaction is a crowdfunding offering and therefore is a covered security for which the states cannot require registration. Armed with the "insignificant deviations" safe harbor, such issuers may be able to slow or stop state enforcement actions. Similarly, it will be much harder for investors in these offerings to sue for failures to meet the requirements of the exemption if crowdfunding issuers can use the "insignificant deviations" safe harbor to challenge their claims.

The safe harbor is not needed. The rules that apply to crowdfunding are comparatively few, the offerings will be subject to SEC review, and the offerings must be sold by intermediaries that register with FINRA. In view of these requirements and safeguards, it is reasonable to expect compliance with the terms of the exemption as a condition of the exemption.

The safe harbor includes an exception that such an "insignificant deviation" is not a defense to an enforcement action by the SEC. Because the states are likely to be the front line investigator of problems in these offerings, we urge the Commission, at a minimum, to create a parallel exception for enforcement actions by state securities regulators.

The Exemption Should Be Unavailable to Certain Issuers

We urge the SEC to consider making the exemption unavailable to certain types of issuers.

We fully concur with the Commission's determination to make the exemption unavailable to blank check companies. The disclosure gaps inherent in blank check offerings make them fundamentally unsuited for crowdfunding. (Question 19)

We also ask the Commission to make the exemption unavailable to various types of investment vehicles, including real estate funds, oil and gas funds, commodity pools, and vehicles that would hold physical assets such as gold. A 'one size fits all' disclosure form will fail to elicit many important disclosures with respect to these types of issuers. For this reason, we urge that such issuers be excluded from the exemption. (Question 21)

Disclosure and Financial Standards

Many issuers using the crowdfunding exemption will have limited experience in the business they propose to conduct. Based on our interactions with such small business issuers, we expect in many cases that their business plans may not be completely developed and certain aspects of the businesses may not have been considered (*e.g.*, product distribution). Our experience is that these issuers may be unrealistic about the prospects of their business, thereby creating the risk that such issuers may violate the securities laws by omitting material information.

Many investors in these offerings will also have limited experience. These investors may not be able to understand and analyze detailed disclosure materials. They may not be able to ask pertinent questions about crowdfunding issuers and the securities they propose to sell. Crucially, such investors may not have the capacity to determine when information is insufficient or lacking.

In view of these problems, we urge the Commission to emphasize the need for issuers to provide full and fair disclosure to potential crowdfunding investors. The Commission should be prepared to be prescriptive about the kind and amount of disclosure that must be provided.

At this time, we urge the Commission to adhere to the statutory requirements for the financial statements to be provided by issuers, particularly the requirements that financial statements be reviewed or audited by an independent accountant, depending on the amount of the offering. Independent accountants will bring several benefits to these offerings, including: independently and competently evaluating the issuer's financial position, applying uniform and accepted standards (GAAP), and requiring issuers to have adequate financial procedures and systems. Moreover, we anticipate that if independent accountants review or audit the financial statements for these issuers, then the accountants will in some cases prevent false or misleading offerings.

We are not unaware of the costs that the financial statement requirements will impose on early-stage issuers. We also understand that some commenters have raised concerns about the viability of the exemption due to these requirements. In view of this, we understand that the Commission will likely revisit these requirements in the future to determine how their costs balance against their benefits.

SEC Work Plan for Crowdfunding

We commend the Commission for establishing a comprehensive work plan to review and monitor crowdfunding. The information collected by the Commission on these offerings should include: the types of issuers that use crowdfunding; the success of the offerings and issuers; investor gains or losses in these offerings and complaints relating to these offerings and issuers.

We strongly support the Commission's proposal to gather information about jobs created in connection with these offerings and issuers. We also urge the Commission to actively share information about these offerings, and trends relating to these offerings, with the states. These small offerings will have considerable impact in particular states, so timely information about problems will help us protect our citizens. Similarly, the states will often be the first to learn about misleading or fraudulent offerings, therefore we urge the Commission to engage with the states to learn about complaints and problems as they arise.

Strengthen Ongoing Company Reporting

We urge the Commission to strongly emphasize that crowdfunding issuers will be subject to ongoing reporting obligations after the offering is completed and that the Commission will enforce these obligations. Without a meaningful ongoing reporting requirement, investors will have virtually no chance to sell their securities, and participants in any aftermarket for these securities will have no basis to know whether pricing is appropriate. The state securities agencies regularly hear from investors who cannot get basic information from small companies in which they have invested. Without this information, investors cannot know how the company is doing and they cannot know whether they may be entitled to distributions relating to their securities. We urge the Commission to enforce these requirements and to impose meaningful sanctions on companies that fail to report to investors as required.

Reporting States Where Sales are Made

Section 18(c)(2)(F) of the Securities Act allows a state to receive a notice filing with respect to a crowdfunding security if that state is: (i) the issuer's principal place of business or (ii) a state where more than 50% of the crowdfunding securities are purchased. To ensure that the states will receive these notice filings, we urge the Commission to add to Form C-U (offering update form) and to Form C-AR (annual report form) disclosure regarding the states where interests in the offering have been sold and the amount sold in each state. Without such reporting, there will be no mechanism for the states to know whether they are receiving the notices they are entitled to receive under the JOBS Act.

Intermediary-Related Comments:

"Self-Certification" Is Inadequate to Protect Investors and Is Contrary to the Language of the JOBS Act

The proposed rule §227.303(b)(1) allows intermediaries to rely on investor representations concerning compliance with investment limits set by Congress. However, the language of the JOBS Act specifically instructs that an intermediary must "[...] make such efforts as the Commission determines appropriate, by rule, to ensure that no investor in a 12-month period [...] exceed the investment limits set forth in section

4(6)(B)."[1] As currently written, the intermediary has no obligation to ensure that an investor has not exceeded individual investment limits.

The Commission suggests that the JOBS Act allows for investor self-monitoring—an entirely untenable position in light of the high risk and complex nature of investments under the JOBS Act. The Congressional Record makes clear that Congress felt strongly that the majority of investors who will likely participate in crowdfunding offerings may be unable to shoulder this responsibility. In his remarks to the House on March 27, 2012, Congressman Jim Himes noted that the Senate amendment to the House crowdfunding provisions added investor protections to the Bill. Further, he added that this enhanced investor protection was necessary to protect unsophisticated retail investors, who may be incapable of protecting themselves.[2]

In the face of Congressional intent to the contrary, it is inexcusable that the Commission would seek to have investors self-certify that they have not exceeded individual investment limits. We urge the Commission to remove the self-certification provision and to provide alternatively for verification of investment limits and investor net worth through either a third party service or the intermediaries themselves.

The Commission must at least incentivize strong compliance with investor qualification standards. Intermediaries currently have no liability for allowing investments from those who have exceeded their investment limits and strong financial incentive to allow all investments. The Commission should create penalties for intermediaries that fail to meet their duties regarding investment limits. For example, the Commission could impose a fine if it determines that an intermediary had no reasonable basis for believing that an investor met the required qualifications.

The Conditional Safe Harbor for Funding Portals is Directly Contrary to Congressional Intent and May Create Unmanageable Conflicts between Funding Portals and Broker-Dealers

The Commission has created a safe harbor that is overly broad and has created unmanageable conflicts between funding portals and broker dealers. Under §4A(a)(12) of the Securities Act of 1933, Congress instructed the Commission to prescribe further requirements for intermediaries for the protection of investors and in the public interest.[3] In §227.402 of the Commission's proposed rules on crowdfunding, the Commission does precisely the opposite through its creation of a safe harbor for funding portals. Instead of simply applying a clear, black and white list of permitted activities, the Commission creates a safe harbor for funding portals. The safe harbor allows funding portals the freedom to undertake activities outside of those specifically listed in §227.402(b), with no presumption of a rule violation. The Commission has a duty to create rules that protect investors and the conditional safe harbor does not meet this requirement.

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[1] Securities Act of 1933, Sec. 4A(a)(8).
[2] Representative Himes (CT). "Jumpstart Our Business Startups Act." *Congressional Record* 158:50 (March 27, 2012) p. H1586.
[3] Securities Act of 1933, Sec. 4A(a)(12).

The Commission should restrict funding portals to a finite list of activities. There should be no ambiguity or grey areas in regards to the activities funding portals may perform.

Among the enumerated activities permitted to funding portals in §227.402(b) is the ability of a funding portal to pay compensation to a registered broker or dealer. Such compensation is allowed in connection with the sale of any security under the crowdfunding exemption. This provision creates a clear and unmanageable conflict of interest between broker-dealers and funding portals. If this provision remains, investors may be pushed towards unsuitable and risky investments as a result of the commissions paid to the broker/dealer by the funding portals. The provision creates a financial upside for the broker-dealer and funding portal industry, but the downside is placed squarely on the investors and general public. We urge the Commission to remove this conflict, and to prevent funding portals from paying to broker/dealers any type of compensation in connection with the offer or sale of securities under the crowdfunding exemption.

The Proposed Rules Allow Funding Portals to Implicitly Endorse Certain Issuers

Title III of the JOBS Act amends §3(a)(80) of the Exchange Act to define the term "Funding Portal." Included in the definition of a funding portal is the limitation that an intermediary acting as a funding portal may not offer investment advice or recommendations. While the Commission acknowledges that a funding portal may not offer investment advice or recommendations, it fails to adequately enforce this mandate. A funding portal is currently allowed to create "objective" criteria that meet the requirements of the rules, but this may result in the portal implicitly recommending securities.

For example, a funding portal may choose to allow investors to filter opportunities based on the amount of funding already received. This standard is objective, but it will have a strong influence on investors, while also helping the funding portal financially. Investors will be instantly drawn to these offerings, regardless of the merit, when they see the amount already invested. Investors will give more weight to projects already receiving funding (the "wisdom of the crowd"). However, they should not be able to search and base investments on this criterion alone. Intermediaries should instead encourage investors to read disclosure documents and learn about their potential investments. Further, this type of filter creates conflicts for the funding portal, because they will likely be paid based on the success of the offering. Funding portals have a strong incentive to push issuers who are close to meeting funding targets, which will result in payment to the portal.

A funding portal must have no incentive to endorse or favor any offering listed on its site. To avoid such conflicts, the Commission should create a specific list of acceptable objective search criteria, which a funding portal may apply. A list of acceptable criteria will decrease the chance that a potential investor will invest based on an implicit portal endorsement or validation. Additionally, it will eliminate any conflict or incentive for the funding portal to create filters that serve merely to help it maximize profit, and not to

help investors. The Commission must be highly vigilant in this area to ensure that no investors are swayed or influenced by the actions or postings of a funding portal.

Funding Portals Should Not Identify Specific Issuers in Any Advertising Material

Proposed Rule 402(b)(9) allows funding portals to advertise their existence and to identify one or more specific offerings available on the portal. While funding portals should be allowed to advertise, the Commission should not allow funding portals to display specific offerings in their advertising materials. The concern with displaying individual issuers is that investors will interpret this as a recommendation and endorsement of the issuer. Moreover, the provision as written incentivizes funding portals to favor certain opportunities. For example, a funding portal would likely advertise offerings with higher targets that it felt were more likely to be successful, which would in turn make more money for the portal.

The Commission has stated that decisions to include specific offerings in advertisement materials must be based on objective criteria. However, this limitation can be easily circumvented by cleverly using criteria such as "the size of the offering." As an alternative, the Commission should create a more definitive regulation regarding advertising of funding portals that does not reference specific offerings. For example, the rules could allow descriptions of the portals themselves and the specific business segments featured on their websites, without mentioning specific issuers currently registered with the portal.

Responses to Specific Questions in the Proposal

In response to the Commission's numbered questions in the proposal, we provide the following comments:

1: The offering limit for the exemption should be of $1,000,000 gross proceeds, not net proceeds.

5: The definition of "issuer" should include predecessor entities and should also include affiliated issuers. This will prevent an enterprise from carrying out several $1,000,000 offerings by means of affiliates, and thereby evading the offering limit.

8: The Securities Division can agree with the proposal to permit an issuer to rely on the selling intermediary to determine that an investor has not exceeded the investor's annual limit, provided that the issuer has no knowledge otherwise. However, this agreement is conditioned on rules that make clear the duty of the intermediary to ensure that the investor has not exceeded the annual limit, and that provide that this duty cannot be met through a conclusory self-certification by the investor.

15. The Division concurs with the requirement that intermediaries be open to public view. This is consistent with the theory of the exemption, which relies on public analysis of the securities offered for sale.

17 and 18. The Division concurs with the proposal to exclude issuers from using the exemption if they have not met the reporting requirements. Reporting is crucial to protect investors who have purchased crowdfunding securities. For the same reasons, the exemption should exclude affiliates of issuers that have not complied with reporting requirements.

19. The Division strongly supports excluding "blank check" companies from the exemption. The lack of disclosure inherent in the "blank check" approach is fundamentally inconsistent with the principle of obtaining analysis and commentary from the crowd.

21. As stated above, the exemption should not be available to investment vehicles, including real estate vehicles, precious metal funds, currency funds, and commodity pools.

24. The Securities Division supports requiring disclosure about significant employees. This is a main use of proceeds by many companies.

25. It would be helpful for officers and directors to give disclosure about 5 years of business experience, rather than just 3. We believe this should not impose a meaningful financial burden on most issuers.

29 and 30. We ask the Commission to prescribe, or at least provide examples of, disclosures that will meet the requirements of the "description of the business" section.

31. We ask the Commission to prescribe use of proceeds disclosure, or at least provide a list of examples to provide guidance to issuers.

32. Use of proceeds disclosure should be promptly updated upon any material change.

37. The Securities Division supports the Commission's proposal to require disclosure of the terms of the securities being offered, including limits on voting rights, restrictions on transfer, the risk of dilution, and other important matters. These disclosures are crucial for investors to understand the security they are buying.

39 and 40. The Division supports the requirements to specifically identify the intermediary and to disclose the compensation paid to the intermediary. This is clearly material information about the offering.

41. The Securities Division supports requiring legends that address risks of crowdfunding transactions. The Commission should include examples of risk factors the issuer should consider disclosing.

42. The Securities Division strongly supports requiring disclosure of related party transactions. Such transactions can create significant risks in any business, particularly a smaller one.

47 - 49. The Securities Division supports requiring all issuers to provide a narrative discussion of the issuer's financial condition along with disclosure about prior capital raising transactions.

50 - 71. At this time, the Securities Division supports the financial statement requirements under the JOBS Act and the proposed rules. This information will protect investors by providing reliable and accurate disclosure, and in many cases independent accountants will help improve the internal controls and systems at issuer companies. We anticipate the Commission may wish to reevaluate the impact of these requirements once issuers begin to use the crowdfunding exemption.

76 - 79. The Securities Division urges that issuers should promptly report material changes to the information in the offering materials. This requirement is consistent with the principle of the crowd evaluating the offering on an ongoing basis.

80 - 88. As stated above, the Commission should reinforce the obligation of issuers to provide ongoing reports. The reports should be widely available: they should be posted on the EDGAR database and be available through the issuer. Ongoing reports should include a discussion of performance compared to prior periods. As in the initial distribution, accountants should participate in the preparation of reports. The Securities Division also urges that the Commission should not waive the reporting requirement for smaller issuers or when the number of company shareholders falls below a given level.

97 - 104. With respect to the prohibition on advertising, the Securities Division supports a requirement that issuers must file their notices relating to the offering with both the SEC and the intermediary. We support the Commission's proposed form of notice. We also agree that the issuer must identify itself if it participates in the communication channel provided by the intermediary.

105 - 108. Promoters hired by the issuer should register with the intermediary; this information should also be provided to the SEC. This disclosure obligation should apply to all persons who might publicize the offering.

113 - 115. As discussed above, the Securities Division believes the exemption should not be available to investment vehicles. With respect to valuation methodology, the Securities Division warns that valuations based on detailed financial projections from early-stage issuers are likely to have no reasonable basis.

150. The Securities Division supports the requirement that intermediaries clearly disclose the manner in which they will be compensated.

182. The Securities Division supports the unconditional right of investors to cancel an investment commitment for any reason until 48 hours prior to the close of an offering.

236. The Securities Division supports the proposal that funding portals must comply with the same privacy rules that are applicable to brokers. Such rules should enhance investor confidence in these internet-based offerings.

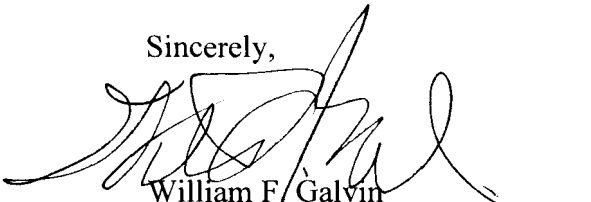
279. The Securities Division supports the Commission's application of "bad actor" disqualifications to both issuers and funding portals.

Conclusion

We urge the Commission to adopt final rules that will apply rigorous disclosure standards to issuers and that will protect investors when they deal with intermediaries. We also urge the Commission to remove the substantial compliance safe harbor from the exemption. It is also our view that certain types of issuers will not fit well in the crowdfunding model, and that they therefore should be excluded from the exemption.

Thank you for your consideration of these comments. If you have questions or we can assist in any way, please contact me or Bryan Lantagne, Director of the Massachusetts Securities Division at (617) 727-3548.

Sincerely,



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