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January 18, 2016

Via Electronic Mail at rule-comments@sec.gov

Honorable Mary Jo White, Chair
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549

Re: Comments on Proposed Rule: *Amendments to Facilitate Intrastate and Regional Securities Offerings*, SEC Release No. 33-9973; File No. S7-22-15

Dear Chair White:

The undersigned submits the following comments to the Commission in respect of *Proposed Rule: Amendments to Facilitate Intrastate and Regional Securities Offerings*, (Release No. 33-9973; File No. S7-22-15) (the "Release"). In particular, these comments are intended to address the Commission's request for comment on the following:

1. The Initial Regulatory Flexibility Analysis set forth in Section VII of the Release, presented by the Commission pursuant to Section 603 of the Regulatory Flexibility Act of 1980, as amended (the "RFA"), including:

   - Whether the Commission should retain the current Section 3(a)(11) safe harbor under Rule 147, and
   - whether a different, *accelerated* timetable for implementation of certain clarifications to Rule 147 is appropriate.

Though these issues are discussed primarily in the context of the RFA, these comments have equal applicability to issuers which are not small businesses covered under the RFA.

2. Whether the investment limitations under the proposed Rule 147 are appropriate.

This letter also addresses an area not specifically the subject of a request by the Commission for comment:

- the need to conditionally exempt offerings under Rule 147 from the requirements of Section 12(g) of the Securities Exchange Act of 1934, in view of the 500 unaccredited shareholder of record threshold.

This commenter also suggests that the Commission consider extending the 60 day comment period for the Release by at least 45 days. I note the following in this regard:

- this Release was issued on the same day that a nearly 700 page final rules release was issued implementing JOBS Act Title III crowdfunding rulemaking, without any preliminary comment period,
- the original comment period was 60 days, which included year-end holiday vacation time, and
- as of the date of this letter, only 25 comment letters had been submitted.

DISCUSSION

I. The SEC Should Retain the Rule 147 Safe Harbor, With Modifications

A. *The Elimination of the Rule 147 Safe Harbor Would be Disruptive to Ongoing State Offering Activity*

As other commenters have noted (*See* Note 5, *infra*), a growing number of states have enacted crowdfunding exemptions in express reliance on Section 3(a)(11) of the Securities Act of 1933 (the "Securities Act") and the safe harbor under the existing safe harbor, Rule 147. Therefore, eliminating the Section 3(a)(11) safe harbor in its entirety would be disruptive to the ongoing utilization of these exemptions and would unnecessarily require further state level legislation and/or regulatory rulemaking in order to ensure the continued, uninterrupted ability to use these exemptions in the manner contemplated by the Release.

Having said that, in view of existing statutory impediments to making some of the proposed changes incorporated into the proposed Rule 147[1], such as the statutory requirement under Section 3(a)(11) that a corporation or other entity be organized in the state where the offering is conducted, though the existing Rule 147 ought to remain in place for a variety of reasons as a safe harbor under Section 3(a)(11), there are compelling reasons to adopt a new, expanded intrastate exemption as a supplement to the Rule 147A safe harbor under the Commission's statutory powers under Section 28 of the Securities Act.

B. *The Elimination of the Existing Rule 147 Safe Harbor Would be Unduly Burdensome to Small Issuers*

The proposed elimination of the Rule 147 safe harbor under Section 3(a)(11) of the Securities Act under the circumstances contemplated by the Commission raises important issues under the Regulatory Flexibility Act of 1980. As the Commission notes in the Release:

[1] For the sake of clarity, the existing Rule 147 is sometimes referred to in this letter as "Rule 147"; and Rule 147, as proposed to be amended, is sometimes referred to in this letter as Rule 147A.

> The Regulatory Flexibility Act directs us to consider significant alternatives that would accomplish the stated objectives of our amendments, while minimizing any significant adverse impact on small entities. Specifically, we considered the following alternatives: (1) establishing different compliance or reporting requirements ***or timetables*** that take into account the resources available to small entities; (2) **clarifying,** consolidating or simplifying compliance and reporting requirements for small entities under the rule; . . . .[2]

[Emphasis added]

For the reasons discussed below, the Commission ought to retain Rule 147 as a Section 3(a)(11) safe harbor, albeit with appropriate clarifications and modifications. Further, the Commission ought to ***clarify*** the scope of existing Rule 147 as regards the scope of permissible internet solicitation under both Section 3(a)(11) and Rule 147, albeit ***on a more accelerated timetable*** than currently proposed.

1. *Section 3(a)(11) is Not an Adequate Substitute for the Elimination of Existing Rule 147*

Section 3(a)(11), absent a "safe harbor" rule, is essentially of little or no practical value to small issuers and others who seek to rely on this exemption.[3] Currently, Rule 147 is the only safe harbor, and has been for more than 40 years. Hence, eliminating Rule 147 in its entirety, with only Section 3(a)(11) left in its place, would be of little or no value to small issuers. As one noted scholar has pointed out:

> "Although Rule 147 is not the exclusive manner in which an issuer may qualify for an exemption under Section 3(a)(11), see 17C.F.R. § 230.147, Preliminary Note 1 (2005), the common law under that Section is so unsettled and undeveloped that it does not provide a workable vehicle for the sale of securities."[4]

Nor is the proposed Rule 147A an adequate substitute for a Section 3(a)(11) safe harbor. As noted above, as pointed out by numerous commenters on the Release's proposed changes, in view of the reliance by a large, growing number of states on both Section 3(a)(11) and Rule 147 in adopting intrastate crowdfunding exemptions, the practical effect of adopting a new Rule 147A in substitution for Rule 147, which does not rely on Section 3(a)(11) and Rule 147, would be unnecessarily disruptive to small issuers.[5] Hence, simply adopting new Rule 147A would not

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[2] *See* Release, at p. 155.

[3] *See* Note 30 to *Proposed Rule Amendments to Facilitate Intrastate and Regional Securities Offerings*, SEC Release No. 33-9973 (the "Release"): " Issuers that seek guidance on how to comply with Section 3(a)(11) after the adoption of any final rules amending Rule 147, as proposed, would continue to be able to rely on judicial and administrative interpretive positions on Rule 147 issued prior to the effectiveness of any such final rules."

[4] Rutherford B Campbell, Jr., *Regulation A: Small Businesses' Search for "A Moderate Capital"*, 31 Del. J. Corp. L. 77, note 72 (2006) (the "Campbell Article")

[5] *See, e.g.*, Judith M. Shaw, President, NASAA and Maine Securities Administrator (January 11, 2016); Anthony J. Zeoli, Partner, Freeborn & Peters LLP (November 5, 2015); Sara Hanks, CEO, CrowdCheck, Inc. (January 2,

be an adequate substitute for retaining the existing Rule 147, especially when incorporating *limitations* nowhere to be found in Section 3(a)(11). Of course, as discussed below, Rule 147A would be a useful *adjunct* to the Rule 147 safe harbor.

Moreover, the somewhat schizophrenic manner in which the Commission has interpreted the bounds of Section 3(a)(11), particularly on the issue of the scope of internet solicitation, stands as a testament to the perils of relying upon Commission or administrative pronouncements in lieu of clear and unambiguous guidelines, even for the most sophisticated securities professional. Case in point: As discussed below, as of 1999 it seemed to be a safe bet to the most seasoned securities practitioner to be able to utilize unrestricted internet solicitation under Section 3(a)(11), albeit with an appropriate legend restricting the pool of offerees. Indeed, as of 2006 at least one highly respected scholar apparently thought he was safe in relying upon prior SEC rulings in reaching this conclusion.[6] But according to the Staff in 2014, what seemed to have been a safe bet in 2006 turned out to be a losing bet in 2014.[7]

Furthermore, many of the changes proposed in Rule 147A can be accomplished by simply clarifying or modifying Rule 147 while retaining it as a safe harbor for Section 3(a)(11). Most notable is the current limitation in Rule 147 regarding the manner of offers in an offering under Section 3(a)(11) of the Securities Act. Indeed, many other of the proposed changes embodied in Rule 147A would also fit within the boundaries of Section 3(a)(11) if the Commission simply added many of these changes to the existing Section 3(a)(11) safe harbor.

2. *There are Less Burdensome Alternatives Available to the Commission than Eliminating a 40 Year Old Safe Harbor in its Entirety – A Simple Clarification to Rule 147 Allowing the Use of the Internet for Offers Would Go a Long Way.*

The Release, and proposed Rule 147A, address a major limitation on the usefulness of current Rule 147, especially as the foundation for intrastate investment crowdfunding. Specifically, though not mentioned in the Release, in 2014 the Staff on two occasions interpreted Rule 147 in a manner that severely restricts a single form of media, *i.e.* the internet, in connection with the solicitation of offers under Rule 147, even when accompanied by a conspicuous legend indicating that offers are made only to residents of a particular state.[8] However, to conclude, as the Commission appears to do, that the only solution to *this* problem is to create a new rule which does not rely upon Section 3(a)(11) appears to be erroneous.[9] There

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2016); Kim Wales, CEO, Wales Capital, and Executive Board Member, CFIRA, New York, New York (January 11, 2016).

[6] *See* Campbell Article, at notes 75, 78.

[7] *See* Compliance and Disclosure Interpretations: Securities Act Rules, U.S. SEC.& EXCH. COMM'N, Questions 141.04 and 141.05 (the "2014 CDIs")

[8] *See* the 2014 CDIs."

[9] *See, e.g. Release, at p. 7:* "The proposed amendments would eliminate the ***current*** restriction on offers, while continuing to require that sales be made only to residents of the issuer's state or territory."[Emphasis added.]. This commenter notes that the only "current restriction" of which he is aware is contained in a 2014 Staff level interpretation which is by its terms not binding upon the Commission, and has yet to be explicitly addressed by the Commission, even within the confines of this Release. In fact, there is not even a mention of the 2014 CDIs (Note 7, *supra*) in the Release. Therefore, the predicate analytical foundation required by the RFA in this regard appears to be absent from the Release.

is ample authority indicating that the Commission has the power under Section 3(a)(11), indeed the obligation, to allow unrestricted offers on the internet ***where appropriately legended to restrict offers to residents of a single state***.

Some of this authority is cited in the Release itself. *See, e.g.,* Securities Act Release No. 33-4434, Fed. Sec. L. Rep. (CCH) 2270, at 2609 (Dec. 6, 1961) (stating that offers under Section 3(a)(11) "may be made the subject of general newspaper advertisement [provided the advertisement is appropriately limited to indicate that offers to purchase are solicited only from, and sales will be made only to, residents of the particular State involved]"), at note 37.

However, other relevant authority is seemingly ignored entirely. Prior to the issuance by the Staff of informal written guidance on this issue in 2014, the issue of the scope of permissible intrastate offers through interstate channels, when appropriately accompanied by limiting legends, the SEC had squarely addressed this issue in a number of no action letters, consistent with prior interpretations by the Commission at different levels. Most recent is *Master Financial*[10], which involved both newspaper and radio advertisements which would be broadcast across state lines. The SEC concluded:

> ". . . the Company will not be disqualified from the use of rule 147 if an out-of-state resident reads or listens to the advertisements. We note that the Company will clearly and conspicuously state in all its advertising and solicitation materials that the offering is intended to be made only to bona fide California residents and that sales will be made only to California residents."

Where there is an appropriate legend, it is difficult to fathom the difference between a newspaper or radio advertisement which unavoidably crosses state lines, and a similar advertisement made over the internet. It seems to me that the inclusion of an appropriate legend satisfies the statutory requirement under Section 3(a)(11) that "offers [be made only to . . .]. It would also be hard to imagine how our Congress back in 1933 would have countenanced, for example, appropriately legended advertisements in a newspaper of wide circulation in New York City's Grand Central Station, while at the same time shunning appropriately legended internet solicitations.

Indeed, one noted scholar and a frequent contributor to the SEC rulemaking public comment forum has concurred with this view, specifically in the context of internet offerings under Rule 147, citing to SEC rulings and interpretations in effect as of the date of that article, 2006),[11] including *Master Financial, Inc*.[12, 13]

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[10] *Master Financial, Inc.*, SEC No- Action Letter, [1999 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶77,560 (May 27, 1999).

[11] Campbell Article, *supra,*, at Note 78:

> " Consider the basic example we have used before-that of a small business that needs to raise a modest $250,000 in equity capital. One could imagine that the CEO of the company could make a broad, general solicitation of investors within the state through advertisements in newspapers, trade journals and even the Internet. *See supra* discussion note 76"

[sic – the reference to note 76 appears to be a mistaken reference to note 75].

[12] Master Financial, Inc. *supra*

And Rule 147A, in important respects, would not be an adequate substitute for Rule 147, even if its scope was limited to the authority granted under Section 3(a)(11). In this regard, as currently proposed, Rule 147A contains both limits on the annual offering amount as well as limitations on amounts that can be invested by an investor. These limitations are nowhere to be found in Section 3(a)(11), and therefore have not been included in the current Rule 147. Moreover, as discussed elsewhere in this letter, there does not appear to be any cogent reason for the Commission to impose these limitations upon states at the federal level. Indeed, these limitations, coupled with the proposed elimination of a Rule 147 safe harbor, could rightly be viewed as a backhanded attempt by the Commission to supplant the judgment of state legislatures and state securities regulators in the intrastate crowdfunding arena.

3. *Clarification of the Scope of Permissible Internet Solicitation under Section 3(a)(11) and Rule 147 Ought to be Made by the Commission With Reasonable Dispatch, and Ought Not to Wait on Implementation of Final Rules by the Commission.*

In this commenter's view, the Commission unnecessarily mooted intrastate crowdfunding for those states relying upon Section 3(a)(11) and Rule 147 by allowing a 2014 written informal rule interpretation at the Staff level (*i.e.*, the 2014 CDIs) to stand for even this long a period of time, in the face of not only substantial authority *by the Commission* to the contrary, but also the expressed concerns of both state regulators and market participants.[14] And the damage done, which continues to be done, is palpable. Indeed, arguably the Commission is compounding this "sin" by now proposing to eliminate long standing statutory and regulatory underpinnings for intrastate crowdfunding affecting a large number of states and their residents. Moreover, the Commission ought not to raise the specter of *scienter* by holding necessary and long overdue clarifications to the scope of Section 3(a)(11) and Rule 147 hostage to the imposition of mandatory investment caps, either on small issuers or unaccredited investors – a *Faustian* bargain which our states and their constituents can ill afford.

Accordingly, this commenter believes that the Commission should reconsider its analysis of the scope of the existing Rule 147 and Section 3(a)(11) of the Securities Act, as concerns the ability of an issuer to utilize internet solicitation with an appropriate restrictive legend.[15] And in

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[13] *See, also: See, e.g.*, Samuel S. Guzik, *"JOBS Act Crowdfunding in 2016 – It's Time to Connect the Dots," CrowdfundBeat*, November 11, 2015 (http://crowdfundbeat.com/2015/11/09/jobs-act-crowdfunding-in-2016-its-time-to-connect-the-dots-in-this-new-era/); Samuel S. Guzik, "*Intrastate Crowdfunding at Risk." CrowdfundInsider*, July 14, 2014, http://www.crowdfundinsider.com/2014/07/43119-intrastate-equity-crowdfunding-risk/.

[14] By way of example, these concerns were discussed in a meeting with then SEC Commissioner Daniel M. Gallagher in June 2014, and again on December 17, 2014, in a meeting with Ted Yu, in his capacity as representative of the Office of the SEC Chair. The latter meeting specifically addressed the concerns of three state securities regulators, in addition to the concerns of this commenter.

[15] This commenter notes the recommendation of the SEC Advisory Committee on Small and Emerging Companies, upon which the Release expressly relies in part to expand the scope of Rule 147. The stated premise of this recommendation is as follows:

> 4. There are three identified areas that currently make it difficult for issuers to use Rule 147: "The rule does not allow offers to out-of-state residents; therefore, an offering placed on a publicly-available website or actively promoted on social media and viewable by out-of-state residents ***is impermissible under the rule.***

the event the Commission concurs with the analyses of this issue, the Commission ought to act with reasonable dispatch to clarify the public record on the permissible scope of internet solicitation under Section 3(a)(11) of the Securities Act without waiting on the completion of final rulemaking under the Release.

II. Adoption of a New Rule 147A, in Tandem with an Updated Rule 147, Would be of Tremendous Benefit to Small Enterprise Capital Formation

As the Release recognizes, there clearly are statutory limitations on the usefulness of the Section 3(a)(11) exemption – though, as argued in this letter, allowing the use of the internet is not one of these limitations. As noted in the Release, Section 3(a)(11) was adopted in 1933. Business practices have changed dramatically since then. To the extent that the Release addresses these statutory limitations through the use of its rulemaking powers under Section 28 of the Securities Act, and also incorporates changes to other problematic aspects of current Rule 147, the adoption of Rule 147A would be expected to create a useful alternative to small enterprises to raise capital, albeit with one important *caveat* – the Commission ought not limit the power of the 50 state legislatures to determine what is best for its citizens, particularly in the evolving area of investment crowdfunding, under the guise of the mantra of "modernizing" Rule 147.

Usurpation of State Authority to Set Limits on Amounts Raised or Invested is Inappropriate.

Certain aspects of Rule 147A, as proposed, are problematic, particularly those aspects of Rule 147A which usurp the power of state legislatures and state regulators to determine what best suits the needs of their states' constituents, and to be able to respond to changing conditions without the necessity of petitioning either the Commission or Congress. By implementing these limitations under the guise of "modernizing" Rule 147 could rightly be viewed as the Commission imposing its judgment on the judgment of the states in the relatively new, and rapidly evolving, area of investment crowdfunding.

Specifically, Rule 147A, as proposed, imposes caps on both the amounts an issuer can raise as well as the amounts an investor can invest. As noted above, there is simply no cogent reason that can be posited for the Commission to substitute its judgment for the judgment of the individual states.

This is an impediment in the age of the Internet and social media. . . ." http://www.sec.gov/info/smallbus/acsec/acsec-recommendation-modernize-rule-147.pdf [Emphasis added.]

However, based upon a review of the Commission's record of the Advisory Committee deliberations on this issue it appears that the Advisory Committee failed to consider *any* precedent which would support the conclusion that internet solicitation *would in fact be permissible* under the current Rule 147. *See* Transcript of Meeting of Advisory Committee on June 3, 2015, *http://www.sec.gov/info/smallbus/acsec/acsec-transcript-060315.pdf.*

Apart from states being in the best position to determine what is best for their residents, be it as entrepreneurs, small business owners or investors, when compelling federal interests are not triggered these monetary limitations will unnecessarily impinge on the ability of states to experiment with different crowdfunding regimes. And experimentation by the states in the context of investment crowdfunding is clearly the order of the day. Both our Congress and the Commission would be able to better assess the efficacy of investment crowdfunding generally if they have the benefit of reliable historical data at the state level. This would be both a useful and welcome substitute for rampant speculation, even well reasoned opinions, when unsupported by reliable data. Indeed, at a recent speech delivered by U.S. Congressman Patrick McHenry[16], the original Congressional sponsor of what ultimately was ultimately adopted, with modifications, as Title III of the JOBS Act, he remarked that the fate of further Congressional action to improve and enhance Title III can be expected to depend in large part on data emanating from operational investment crowdfunding markets.

There are many divergent opinions on the efficacy of investment crowdfunding and the suitable parameters to ensure a balance between investor protection and capital formation. So let's allow our 50 states to put some meat on these bones, without any unnecessary interference by the Commission, where only the interests of their states' residents are invoked. No federal interests appear to be at play, given the proposed scope of Rule 147A – limited to local businesses and local investors. There is ample "adult supervision" at the state level without needlessly imposing a federal "nanny" and its views on all 50 states – handcuffing state legislatures and state regulators to determine what is in the best interests of their constituents and their local economies. Moreover, to the extent federal regulatory oversight is deemed necessary, the significant and far reaching enforcement powers of the Commission under Section 10(b) and Rule 10b-5 of the Securities Exchange Act of 1934 remain fully intact.[17]

III. The Commission Should Consider the Modification of Reporting Obligations under Section 12(g) of the Securities Exchange Act of 1934 as Part of the Rule 147 and Rule 147A Rulemaking.

Absent from the Release is any discussion, or even a mention, of current requirements under Section 12(g) of the Securities Exchange Act of 1934 (the "1934 Act"). Two Release commenters have raised this issue, however, and rightly so.

It is contemplated by the Release that Rule 147A may have great vitality in the area of investment crowdfunding, which appeals to a large extent to unaccredited investors. Absent exemptive action by the Commission an issuer with more than $10 million in assets and more

[16] Unpublished remarks delivered by Congressman Patrick McHenry at the Crowdfunding Professional Association 2015 Annual Summit on December 2, 2015, in Washington, D.C.

[17] Though not specifically proposed in the Release, the Commission has requested comment on the requirement that an intermediary be required as a condition to the utilization of Rule 147A. Again, the wisdom of this requirement ought to be left to the judgment of the states' legislatures and securities administrators. Though an intermediary can afford a measure of investor protection, the requirement of an intermediary imposes additional financial costs on an issuer, and also eliminates the ability of an issuer to go it alone, as many states now allow.

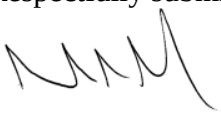
than 500 unaccredited shareholders of record may inadvertently become a fully reporting company under the 1934 Act. Absent an appropriate exemption from Section 12(g) for both Rule 147 and Rule 147A securities, this limitation alone could have a chilling effect on the ability of small issuers to utilize investment crowdfunding at the state level.

By the same token, having a 500 shareholder threshold would have the untoward effect in many cases of requiring issuers to impose a higher investment minimum for investors in an offering to reduce the number of total investors. With higher minimum investment levels, some prospective unaccredited investors would simply not participate in the offering – reluctant or even unable to make the minimum required investment. Others might be encouraged to invest more than might be appropriate for them to risk in a highly speculative, but otherwise worthwhile investment. This result is inconsistent with notions of investor protection. And on a more fundamental, philosophical level, it goes against the grain of the very foundation of crowdfunding – the investment of *small* amounts of money by a large group of people, a/k/a "the crowd" – facilitated with great speed and reduced expense by the internet.

The Commission has both vetted and addressed this issue in the context of federal "JOBS Act" Title III crowdfunding. The same policy considerations and concerns which motivated both Congress and the Commission in this area ought to be applicable in the context of Rule 147A and Rule 147, which can be expected to continue to be the primary federal enabling foundation for intrastate crowdfunding.

I would be pleased to discuss these matters further at your convenience.

Respectfully submitted,



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