



CrowdFund Intermediary Regulatory Advocates
1345 Avenue of the Americas
New York, NY 10105
Telephone: (212) 370-1300

January 26, 2014

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

**Re: File No.: S7-09-13; Section II.B.1, “Disclosure Requirements – Financial Disclosures”;
Release 33-9470**

Dear Ms. Murphy:

I am writing you on behalf of the Crowdfund Intermediary Regulatory Advocates (“CFIRA”), a crowdfunding trade organization that lobbies and advocates for regulations that will support the crowdfunding industry in connection with Title II and Title III of the Jumpstart Our Business Startups Act of 2012. CFIRA’s role is to protect the interests of investors and issuers, and advance the common business interest of intermediaries and third party service providers in the securities industry. Our members comprise intermediaries (broker-dealers and funding portals), issuers, investors, and third party service providers who are engaged in, or who intend to engage in, business under Titles II and III.

This letter is written in response to the Proposed Rules for Section 4A(b)(1)(D) that requires “a description of the financial condition of the issuer.” It also establishes a framework of tiered financial disclosure based on aggregate target offering amounts and all other offerings made in reliance on Section 4(a)(6) within the preceding 12-month period:

- Issuers offering \$100,000 or less are required to file with the Commission, provide to investors and the relevant intermediary and make available to potential investors income tax returns filed by the issuer for most of the recently completed year (if any) and financial statements that are certified by the principal executive to be true and complete in all material respects;
- Issuers offering more than \$100,000, but not more than \$500,000, are required to file with the Commission, provide to investors and the relevant intermediary and make available to potential investors financial statements reviewed by a public accountant that is independent of the issuer.
- Issuers offering more than \$500,000 (or such other amount as the Commission may establish) are required to file with the Commission, provide to investors and the relevant intermediary, and make available to potential investors, audited financial statements.



Crowdfunder Intermediary Regulation Advocates

This level of financial disclosure for capital raises of more than \$500,000 will be a severe impediment for small business when many will have limited financial resources to absorb the expense prior to raising capital using Crowdfunding.

CFIRA understands that the three tiered financial disclosure requirements are statutory and that the raised-based audit requirements are in the law as defined by Congress. The language used in the Proposed Rules suggest that Congress may have given the SEC discretion with respect to modifying these requirements and we urge the SEC to utilize this discretion. Moreover, if the SEC decides against exercising this discretion, CFIRA as an organization is prepared to seek legislative guidance on this issue, given its importance.

We ask you to consider “what is the purpose of financial audits?” We call your attention to the requirements from the Small Business Administration’s Section 8(a) program; following are the financial data disclosure standards based on annual gross receipts (versus the amount of capital being sought by the issuer) which offer an alternative approach to the financial disclosure guidelines.

1. Audited annual financial statements from a licensed independent public accountant for those concerns with actual receipts of more than \$10,000,000 or more. Statements must be submitted within 120 days after the close of the firm’s fiscal year. Financial data must always be signed and dated by the C.E.O., President or sole owner.
2. Reviewed annual financial statements from a licensed independent public accountant for those concerns with gross annual receipts of \$2,000,000 to \$10,000,000. Statements must be submitted within 90 days after the close of the firm’s fiscal year.
3. Annual statements verified as to accuracy by the proprietor or an authorized officer, for those concerns with actual gross annual receipts less than \$2,000,000.
4. Quarterly un-audited statements when required, verified as to accuracy by the proprietor, a partner or an authorized officer regardless of amount of gross receipts, which may be prepared internally or by an independent qualified public accountant.
5. Audited or reviewed annual and/or quarterly statements may be required from a licensed independent public accountant when the SBA decides it is vital to obtain a more thorough verification of a concern’s financial position. Such as when a concern’s capacity to perform specific 8(a) contract must be determined or when needed to determine continued program eligibility.
6. Less than \$2,000,000 must submit prepared in-house or compiled statements. Statements must be submitted within 90 days of the close of the firm’s fiscal year.¹:

The Commission requested comments on the proposed rules that span areas concerning accounting, ongoing reporting, disclosure and fraud in Section II.B.1 and we have provided the following recommendations for each question as outlined.

Question 47. *Are these proposed requirements for the discussion of the financial condition of the issuer appropriate? Why or why not? Should we modify or eliminate any of the requirements in the*

¹ <http://www.sba.gov/sites/default/files/Participation%20Agreement%2011%207%2011.pdf>

² http://www.aicpa.org/Research/Standards/AuditAttest/ASB/Documents/Mtg/1207/2012_07_ASB_Item3B.pdf

proposed rule or instruction? If so, which ones and why? Should we require any additional disclosures? If so, what disclosures and why? Should we prescribe a specific format or presentation for disclosures?

Recommendation: The proposed requirements are appropriate. Certain disclosures allow an investor to evaluate in more depth the potential investment rather than by reviewing tax returns or financial statements alone. The disclosure requirements for smaller raises would be appropriate, as the investor will use this information equally regardless of the size of the offering.

We also are supportive of the requirement for issuers with no prior operating history to include disclosure when there is no or limited operating history, in addition to providing relevant information disclosures focused on financial & operational milestones and other life cycle hurdles. Issuers with robust operating history should include this as another form of disclosure. Each company's experience is varied, and prescribing a specific format could diminish the value of such disclosures and make them cookie-cutter compliant rather than providing useful and pertinent information regarding the company's financial condition and plans.

Question 50. *Under the statute and the proposed rules, issuers are required to file with the Commission, provide to investors and the relevant intermediary and make available to potential investors financial statements. The proposed rules would require all issuers to provide a complete set of financial statements (a balance sheet, income statement, statement of cash flows and statement of changes in owner's equity) prepared in accordance with U.S. GAAP. Should we define financial statements differently than under U.S. GAAP? If so, what changes would be appropriate and why? What costs or challenges would be associated with the use of a model other than U.S. GAAP (e.g., lack of comparability)? What would be the benefits? Please explain.*

Recommendation: Issuers should be allowed to provide financial statements in accordance with special purpose frameworks, as allowed by AICPA AU-C Section 800, *Special Considerations—Audits of Financial Statements Prepared in Accordance With Special Purpose Frameworks*,² as such statements are more cost efficient, and provide investors with sufficient comparable information about the financial condition of early stage enterprises. Imposing a more costly financial statements requirement will potentially prevent smaller companies from utilizing the capital formation advantages of securities crowdfunding. The JOBS Act was intended to facilitate raising capital for small and emerging companies through public funding while maintaining investor protections. Elevating the financial reporting standards will have a contrary effect, without gains in investor protections.

There are other comprehensive accounting frameworks that may yield the same result for investors as GAAP but with a lower barrier for small and emerging businesses. In the current marketplace, users of financial statements are seeking such alternative bases of presentation to lower cost. This is evidenced by the proliferation of tax basis financial statements in recent years as U.S. GAAP appears to have become increasingly complex. Further, the FASB and the AICPA have responded to this trend by each creating significant changes affecting the middle market. The FASB created the Private Company Council in 2012, which recently released several Accounting Standards Updates (ASUs) that reduce some of the complex requirements for non-registrants by allowing

² http://www.aicpa.org/Research/Standards/AuditAttest/ASB/Documents/Mtg/1207/2012_07_ASU_Item3B.pdf

them to make certain simpler accounting policy elections.³ In addition, the AICPA has put forth the Financial Reporting Framework (FRF) for Small- and Medium-Sized Entities (SMEs)⁴, which is an altogether different basis of accounting than U.S. GAAP that small- and medium-sized entities can choose to use. Based on this trend in the market, we suggest that issuers be allowed to utilize any reporting framework that meets SEC, FASB or AICPA standards of an allowable reporting framework.

Question 51. *Should we exempt issuers with no operating history or issuers that have been in existence for fewer than 12 months from the requirement to provide financial statements, as one commenter suggested? Why or why not? Specifically, what difficulties would issuers with no operating history or issuers that have been in existence for fewer than 12 months have in providing financial statements? Please explain.*

Recommendation: Issuers with no operating history or that were in existence for fewer than 12 months should be exempt from the requirement to provide financial statements, since financial statements of an entity with little to no operating performance would provide minimal information to investors, but would add the cost of an audit or review to the expenses of launching a crowdfunding campaign. Such a burden is not consistent with the intent of the JOBS Act.

We also are supportive of the requirement for issuers with no prior operating history to include disclosure that there is no or limited operating history, and then include discussion focused on financial milestones and operational, liquidity and other life cycle hurdles.

We all agree on the importance of creating robust investor protection standards for the Crowdfunding Industry while improving capital formation and job creation. However, imposing the requirement of financial statements prepared, reviewed, or audited in accordance with US GAAP on small business issuers, that in some cases have little to no cashflow, may yield the unintended consequence of issuers seeking funding solely from accredited investors using Regulation D, Rule 506(c) rather than utilizing Regulation Crowdfunding given the more arduous requirements and higher out-of-pocket expenses required for compliance with Regulation Crowdfunding. This would artificially exclude unaccredited investors from these investment opportunities.

We recommend that the Commission allow the industry to develop into a healthy marketplace by allowing issuers to utilize any reporting framework that meets SEC, FASB or AICPA standards of an allowable reporting framework. It is an option worth exploring as the U.S.A. readies to open the securities based Crowdfunding industry in 2014.

Working alongside the Commission, CFIRA strives to develop a balanced and healthy ecosystem for the crowdfunding industry. We believe that this will be possible, so long as flexibility, transparency, and a comprehensive framework of industry standards and best practices are created as the industry matures. The members of CFIRA remain available for further discussions relating to defining the final rules for Title III and we continue to be available to work

³ <http://www.fasb.org/pcc/news>

⁴ <http://www.aicpa.org/InterestAreas/FRC/AccountingFinancialReporting/PCFR/DownloadableDocuments/FRF-SME/FRF-SMEs-Framework.PDF>



with the Commission, to ensure a healthy ecosystem, enhance capital formation, and focus on investor protection.

Respectfully submitted,

Kim Wales
Wales Capital, Founder & CEO
CFIRA, Executive Board Member
CF50, Board Member