State of California
Office of the Attorney General
XAVIER BECERRA
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September 24, 2019

VIA ELECTRONIC SUBMISSION

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

RE: Concept Release on Harmonization of Securities Offering Exemptions, Release No. 33-10649, File No. S7-08-19

Dear Secretary Countryman:

On behalf of the undersigned Attorneys General, we write to comment on the Securities and Exchange Commission's ("SEC") Concept Release on Harmonization of Securities Offerings Exemptions, Securities Act Release Nos. 33-10649, 34-86129, IA-5256, IC-33512 84 Fed. Reg. 30,460 (released June 26, 2019) ("Concept Release" or "Release"). We appreciate this opportunity to provide comments as the SEC considers modifications to exemptions from registration under federal securities laws. Because California is one of the largest markets for most categories of exempt offerings, we are particularly concerned about promoting the integrity of those transactions.

I. SUMMARY

We recognize that exemptions from registration can be an effective way for issuers—particularly small or early-stage issuers—to raise capital without the expense and burden of registration. But the Concept Release and the SEC studies that we have reviewed offer almost no data on the outcomes for investors or issuers who participate in exempt offerings, nor do they address retail investors'[1] interest, if any, in participating in

[1] We use the term "retail investor" to mean individuals who invest primarily for personal, family, or household purposes. *See* 17 C.F.R. § 240.15*l*-1(b)(1)(B).

exempt offerings.[2] Instead, the Concept Release focuses almost exclusively on issuers' access to capital from an undifferentiated population of investors. Without data about investor and issuer outcomes or retail investor demand for exempt offerings, the SEC cannot adequately evaluate how the current exemption framework is operating, much less propose significant changes to that framework. We recommend that before making any modifications to the current exemptions, the SEC gather data on issuer and investor outcomes as well as retail investor demand for exempt offerings, and analyze how the current framework is impacting each of those categories. Only armed with those analyses will the SEC be able to prudently make reforms.

Registration of securities—whether at the state or federal level—ensures access to ongoing material disclosures from issuers, which aids investors in making informed decisions. Exemptions from federal registration, and the concomitant requirements of significant initial and ongoing disclosures, should generally be limited to situations where investors are sophisticated and powerful enough to demand (and receive) pertinent information from issuers. To the extent that less sophisticated investors are permitted to participate in exempt offerings, we believe that issuers should be required to provide them with greater disclosures of material information.

We write to encourage the SEC to gather further data on investor outcomes before making any changes to the current framework. We emphasize the importance of the current restrictions on exempt offerings for the protection of investors. We encourage the SEC to weigh the importance of investor protection against any claims by other stakeholders that these restrictions should be loosened.

II. COMMENTS

A. State-Level Investor Protections Are Crucial.

We appreciate the SEC's recognition throughout the Concept Release of the importance of state-level investor protections, particularly the role of states in anti-fraud enforcement. *See, e.g.*, Concept Release at 30,483, 30,491, 30,504, 30,510. As has been

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[2] *See* Staff, Sec. & Exch. Comm'n, *Report to the Commission: Regulation Crowdfunding Study* 17-18, 42-45 (2019), https://www.sec.gov/files/regulation-crowdfunding-2019_0.pdf (hereinafter "*SEC Regulation Crowdfunding Study*"); *see generally* Scott Bauguess, et al, Div. of Econ. & Risk Analysis, Sec. & Exch. Comm'n, *Capital Raising in the U.S.: An Analysis of the Market for Unregistered Securities Offerings, 2009-2017* (2018), https://www.sec.gov/dera/staff-papers/white-papers/dera_white_paper_regulation_d_082018 (hereinafter "*SEC Analysis of Capital Raising in the U.S.*"); Letter from Rick A. Fleming, Investor Advocate, Sec. & Exch. Comm'n to Vanessa Countryman, Secretary, Sec. & Exch. Comm'n (July 11, 2019), https://www.sec.gov/comments/s7-08-19/s70819-5800855-187067.pdf (hereinafter "*Investor Advocate Letter Re: Concept Release*").

often observed, states are the "cops on the beat" and often are at the forefront of identifying and taking action against schemes to exploit investors.[3] As the SEC acknowledges in the Concept Release, state anti-fraud enforcement power is key to ensuring that investors are protected, whether in the public or private markets. *See, e.g., id.* at 30,483.

B. The SEC Should Study Investor And Issuer Outcomes In Exempt Offerings Before Modifying The Current Framework.

Before making changes to any of the current exemptions from federal registration, the SEC should study investor and issuer outcomes in exempt offerings. The Concept Release offers essentially no data about how investors—especially retail investors—fare in exempt offerings, nor does the Release include any data about the results for issuers. The Commission's 2018 analysis of unregistered securities offerings and its recent study of offerings under Regulation Crowdfunding ("Reg CF") similarly suffer from a lack of data about results for investors or issuers.[4]

Without data about investor outcomes, the SEC may modify a large swath of securities regulation with no information about how that regulation is actually serving investors. And the limited data that is available suggests that purported exempt offerings are often associated with fraud.[5] For example, in the 2013, 2014, and 2015 annual

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[3] *Hearing Before the S. Comm. on Banking, Hous., and Urban Affairs on Efforts to Enforce Sec. Laws, Inv. Adviser Registration & Licensing, State Investigations into Mutual Fund Indus. Abuses, & Inv'r Educ. Programs*, 108 Cong. 884 (2004) (opening statement of Chairman Richard C. Shelby); Letter from Andrea Seidt, Pres., N. Am. Sec. Admin'rs Ass'n, to Elizabeth M. Murphy, Secretary, Sec. & Exch. Comm'n (March 24, 2014), https://s30730.pcdn.co/wp-content/uploads/2011/07/NASAA-Comment-File-S7-11-13-03242014.pdf; Written Test. of Joseph P. Borg, Pres., N. Am. Sec. Admin'rs Ass'n, *Ensuring Effectiveness, Fairness, & Transparency in Sec. Law Enf't: Hearing Before the H. Comm. On Fin. Serv.* (2018), https://www.nasaa.org/wp-content/uploads/2018/06/Written-Testimony-of-NASAA-President-Joseph-Borg-HFSC-CM-Hearing-June-13-2018.pdf.

[4] *See generally SEC Analysis of Capital Raising in the U.S.*, *supra* note 2; *SEC Regulation Crowdfunding Study*, *supra* note 2, at 30 ("We recognize that potential failures to comply with disclosure requirements could pose risks to investors. We cannot assess the general magnitude of such risks in this market due to the limited data available to us at this time.").

[5] *See* Complaint at ¶ 63, *SEC v. Shapiro, et al*, No. 1:17-cv-24624-MGC (S.D. Fla. Dec. 20, 2017) (defendants in alleged Woodbridge Ponzi scheme attempted to avoid registration by limiting investments to "accredited investors"); Jennifer J. Johnson, *Fleecing Grandma: A Regulatory Ponzi Scheme*, 16 Lewis & Clark L.R. 993, 999-1002

enforcement reports issued by the North American Securities Administrators Association ("NASAA"), Regulation D ("Reg D") offerings were listed within the top five "most reported products & schemes."[6]

Before making any modifications, the SEC needs data on how current exemptions affect investors.[7] The SEC should study the differential effects on investor outcomes among the exemption categories, such as, for example, how the disclosure requirements under Regulation A ("Reg A") and Reg CF affect the results for investors in comparison to investors participating in Reg D offerings. The SEC should further investigate the rates of fraud in each category to understand the risks to investors under each exemption. Understanding how the current framework operates for investors is critical to determining the most appropriate modifications for investor protection.

The lack of information about the results for issuers following exempt offerings raises additional concerns. The SEC appears to have little or no data specifically about the outcomes for issuers who pursue exempt offerings.[8] That data could reveal which exempt offering category is most associated with successful issuers. It could also shed light on whether mandatory disclosures have an effect on efficiently allocating capital to issuers that are likely to succeed. In the Concept Release, the SEC notes its concern

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(2012) (describing the MedCap Ponzi scheme involving exempt offerings of promissory notes).

[6] Enf't Section, N. Am. Sec. Admin'rs Ass'n, *NASAA Enf't Report: 2015 Report on 2014 Data* 7 (2015), https://s30730.pcdn.co/wp-content/uploads/2011/08/2015-Enforcement-Report-on-2014-Data_FINAL.pdf (hereinafter *2015 NASAA Enf't Report*); Enf't Section, N. Am. Sec. Admin'rs Ass'n, *NASAA Enf't Report: 2014 Report on 2013 Data* 7 (2014), https://s30730.pcdn.co/wp-content/uploads/2011/08/2014-Enforcement-Report-on-2013-Data_110414.pdf (hereinafter *2014 NASAA Enf't Report*); Enf't Section, N. Am. Sec. Admin'rs Ass'n, *NASAA Enf't Report: 2013 Report on 2012 Data* 8 (2013), https://s30730.pcdn.co/wp-content/uploads/2013/10/2013-Enforcement-Report-on-2012-data.pdf (hereinafter *2013 NASAA Enf't Report*).

[7] Recognizing the importance of such data to SEC exemption rulemaking, a discussion draft of a current House Bill would require the SEC to conduct a study and send a report to Congress before modifying any exemptions or creating any new ones. *See* Staff of H. Comm. on Fin. Serv., 116th Cong., To Require the Sec. Exchange Comm. to Submit a Report to Congress about Private Sec. Offerings, and for Other Purposes (2019), https://financialservices.house.gov/uploadedfiles/bills-116pih-sectsrcapso.pdf. Similar to our suggestions, the draft bill would require the SEC to study the "basis for investor demand for offerings of securities exempt from registration" and the "impact the qualifying modification will have on the likelihood of success of the issuer as a company." *Id.*

[8] *See generally SEC Analysis of Capital Raising in the U.S.*, *supra* note 2; *SEC Regulation Crowdfunding Study*, *supra* note 2, at 44.

about smaller issuers accessing capital, but without data about the results for issuers, it is not clear whether current exemptions result in the efficient allocation of that capital and what changes, if any, may better promote that goal.

The Release acknowledges that the Commission lacks these key data. *See, e.g.*, Concept Release at 30,468. But exempt offerings under Rule 506 of Reg D constitute an overwhelming majority of all exempt offerings, and offerings under that provision require no ongoing reporting.[9] In addition, the current content of Form D and the timing for its filing provides an incomplete picture of the investors who participate in Rule 506 offerings. Information about investor profiles and investor and issuer outcomes for a vast majority of exempt offerings, therefore, is likely very difficult to obtain unless the SEC undertakes to gather it. The SEC could address this problem by requiring additional information about the investors, and ongoing reports detailing how the business is faring and what, if anything, investors have received.[10]

We are concerned that the Concept Release focuses almost exclusively on ensuring the flow of capital to issuers. But the SEC's mission is not only to "facilitate capital formation"; it is also to "protect investors" and "maintain fair, orderly, and efficient markets."[11] To move forward with modifications to the exemption framework without accurate information about issuer and investor outcomes is to make changes in blind pursuit of only one of those goals. Before doing so, the SEC should take steps to gather and analyze data about issuer and investor outcomes.

C. The SEC Should Study Investor Interest In Participating In Exempt Offerings Before Modifying the Current Framework.

In addition to studying the results for investors and issuers in exempt offerings, the SEC should gather data to determine what kind of investors actually want to participate in exempt offerings. SEC Chairman Jay Clayton has noted on several occasions his desire to allow "Main Street" or "Mom-and-Pop" investors to participate in

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[9] *SEC Analysis of Capital Raising in the U.S.*, *supra* note 2, at 8-9; 17 C.F.R. §§ 230.502(b), 506.

[10] That the SEC has the power to impose additional requirements is reflected in its 2013 proposed rule change to the content and timing of Form D (s*ee* 78 Fed. Reg. 44,806, 44,812-816 (proposed July 24, 2013)), as well as the existence of ongoing reporting requirements under Reg A and Reg CF (*see* 17 C.F.R. §§ 230.257(b), 227.202). It would also be extremely useful if issuers that terminate their business were required to file a report detailing how investors were treated during the termination.

[11] "About the SEC," https://www.sec.gov/about.shtml (last visited Sept. 18, 2019).

exempt offerings,[12] but the Concept Release notably lacks any data about whether those individuals want to invest their money in offerings that are often high-risk, illiquid, and have little transparency about the business or its operations.

The Investor Advocate highlighted this issue in his letter to the SEC in response to the Concept Release.[13] The Investor Advocate pointed to the Federal Reserve Board's Survey of Consumer Finance to suggest that companies "may not be able to raise a lot of money from retail investors who do not already fit the definition of accredited investor."[14] That survey shows that a significant majority of households are unlikely to have sufficient surplus income or wealth to invest in highly risky and illiquid exempt offerings. According to the Investor Advocate, participation by retail investors in exempt offerings under Reg A and Reg CF, both of which were structured to allow retail investor participation, has been significantly less than anticipated. By contrast, investment in index funds and exchange traded funds ("ETFs") has grown significantly over the last decade, suggesting that retail investors may be seeking more predictability and liquidity, and less risk, with their investments.[15]

The SEC should investigate this question. The results may reveal that retail investors want to participate in public markets rather than in exempt offerings. If that is the case, the SEC should focus on encouraging more companies to publicly register, perhaps even through higher barriers for exempt offerings. The only way to determine the appropriate course of action is for the SEC to study retail investor behaviors and preferences.

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[12] Jay Clayton, Chairman, Sec. & Exch. Comm'n, *Remarks to the Econ. Club of New York* (Sept. 9, 2019), https://www.sec.gov/news/speech/speech-clayton-2019-09-09 (The SEC should "increase the type and quality of opportunities for our Main Street investors in our private markets."); Dave Michaels, "SEC Chairman Wants to Let More Main Street Investors in on Private Deals," *Wall Street Journal*, Aug. 30, 2018, https://www.wsj.com/articles/sec-chairman-wants-to-let-more-main-street-investors-in-on-private-deals-1535648208 ("Mr. Clayton said the SEC is now weighing a major overhaul of rules intended to protect mom-and-pop investors, with the goal of opening up new options for them.").

[13] Investor Advocate Letter Re: Concept Release, *supra* note 1, at 2-5.

[14] *Id.*

[15] Trevor Hunnicutt, "Index Funds to Surpass Active Fund Assets in U.S. by 2024: Moody's," *Reuters*, Feb. 2, 2017, https://www.reuters.com/article/us-funds-passive/index-funds-to-surpass-active-fund-assets-in-u-s-by-2024-moodys-idUSKBN15H1PN ("Investors are increasingly buying relatively cheap funds that mimic benchmarks…Passive funds currently account for 29 percent of the U.S. market….").

D. The Accredited Investor Definition Should Be Revised To Include A Sophistication Criterion.

The purpose of federal or state registration of securities is to provide all potential investors with equal access to material information about issuers.[16] The goal is to diminish information asymmetries between retail and institutional investors and to promote confidence in public markets.[17] In light of the purpose of securities registration, exemptions to federal registration should be limited to situations in which investors meet two criteria. First, investors should have sufficient sophistication and power to demand (and receive) material information from issuers.[18] Second, investors should have sufficient wealth or income to tolerate illiquidity and withstand losses from their investments. This second criteria could also be satisfied through caps on the amount of investments for individuals who do not meet a certain wealth or income threshold.

The current accredited investor definition requires only one of these criteria: sufficient wealth or income. But when the U.S. Supreme Court first articulated the standard for exemptions to federal registration under Section 4(a)(2), it looked to the sophistication and knowledge of investors, posing the question as whether investors could "fend for themselves." *See SEC v. Ralston Purina Co.*, 346 U.S. 119, 125 (1953). Any modifications to the accredited investor definition should add back this component, and the sophistication requirement for nonaccredited investors under Rule 506(b) could be a good model. Using wealth or income as the only criterion, as the current definition does, sweeps in numerous individuals who lack sufficient knowledge or power to protect themselves against information asymmetries.

E. If Less Sophisticated Investors Are Allowed To Participate In Exempt Offerings, Issuers Should Be Required To Provide Them With Disclosures Of Material Information.

To the extent that investors who do not meet both of our proposed criteria are allowed to participate in exempt offerings, the SEC should require that issuers provide those less sophisticated investors with material information about, for example, the

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[16] Colleen Honigsberg, et al, *Mandatory Disclosure & Individual Inv'rs: Evidence From the JOBS Act*, 93 Wash. U. L.R. 293, 318-19 (2015).

[17] *Id.* at 295.

[18] The requisite power and knowledge do not necessarily stem from finance or business experience or education. Investors who are family or friends with the individuals who manage an issuer may have enough power to demand disclosures and may be close enough to the business to make a sophisticated decision about whether to invest. For exempt offerings where investors lack relationships with the issuers and do not have insight into ongoing operations, however, sophistication and power along the lines of experience or education is more critical.

issuer's financial health, business performance, and capital structure. Investors who are not able to "fend for themselves" should receive the benefit of protection by the SEC through mandatory disclosures.

Mandatory disclosures serve multiple purposes in investor protection. Disclosures provide potential investors with material information about the issuer so they can make an informed decision. Making disclosures mandatory also allows investors to assess the trustworthiness of issuers by looking at their compliance—or lack thereof—offering a simple, bright-line test. Finally, at least one study suggests that mandatory disclosures increase retail investors' confidence in the issuer.[19]

We focus our comments on two exempt offering categories in which California has a particular interest: offerings under Rule 506 of Reg D and under Reg CF. As the Concept Release reflects, California was the state with the largest amount of capital raised under Rule 506 and the largest percentage of Reg CF offerings. 84 Fed. Reg. at 30,485, 30,505. Although we focus on these two categories, we believe that issuer disclosures to less sophisticated investors are critical in all exempt offerings.

1. Rule 506

As noted above, offerings under Rule 506 constitute the vast majority of exempt offerings.[20] In its current form, Rule 506(b) allows up to 35 nonaccredited investors to participate in exempt offerings under the rule, so long as they meet certain sophistication requirements.[21] For any participating nonaccredited investors, Rule 506(b) requires that issuers provide mandatory disclosures.[22] Rule 506(c) does not allow participation by nonaccredited investors.[23] Neither rule requires any disclosures to accredited investors who participate in exempt offerings under the rules (subject to state and federal anti-fraud enforcement).

At the outset, we reiterate our earlier point that there is insufficient data about the outcomes for investors or issuers in Rule 506 offerings. In the absence of that data, the SEC should continue to mandate disclosures to nonaccredited investors that are allowed to participate in exempt offerings under Rule 506(b). Under the current definition, nonaccredited investors have less wealth and income than accredited investors and therefore are at higher risk in the event that they make no return on their investments.

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[19] Honigsberg, *supra* note 16, at 318-19.

[20] *See SEC Analysis of Capital Raising in the U.S.*, *supra* note 2, at 8-9; Concept Release at 30466 (Table 2 listing amounts of capital raised by each type of exempt offering in 2018).

[21] 17 C.F.R. § 230.506(b)(2).

[22] 17 C.F.R. § 230.502(b).

[23] 17 C.F.R. § 230.506(c).

The SEC should ensure that this category of investors receives key information about issuers before making investments.

If the SEC chooses either not to change the current accredited investor definition or to alter the definition in a way that does not include a sophistication criterion, the SEC should modify Rules 506(b) and 506(c) to require issuers to provide mandatory disclosures to accredited investors as well. As discussed previously, the current accredited investor definition sweeps in individuals who lack the sophistication necessary to "fend for themselves" in exempt offerings. And Rule 506/Reg D is often associated with fraudulent investment schemes, making exempt offerings under this category particularly risky.[24] If the SEC continues to distinguish individuals who can participate in exempt offerings solely on their wealth or income, the Commission should at least require issuers to provide mandatory disclosures to protect those individuals who technically qualify as accredited investors but lack the necessary sophistication.

The SEC should also engage in better enforcement of the few existing disclosure requirements under Rule 506 and Reg D.[25] According to one study by the SEC's Division of Economic and Risk Analysis, "Form D filings are not made for as much as 10% of unregistered offerings eligible for relief under Reg[] D."[26] Under Reg D, issuers who fail to file Form D (providing information about their offering) do not lose the exemption.[27] Essentially the only consequence to an issuer for not filing a Form D is the possibility that the SEC could seek an injunction prohibiting the issuer from using the Reg D exemption in subsequent offerings.[28] To avoid this consequence, issuers often file

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[24] *See* Complaint at ¶ 63, *Shapiro,*, No. 1:17-cv-24624-MGC; Johnson, *supra* note 5, at 999-1002; *2015 NASAA Enf't Report*, *supra* note 6, at 7; *2014 NASAA Enf't Report*, *supra* note 6, at 7; *2013 NASAA Enf't Report*, *supra* note 6, at 8.

[25] State securities regulators could be partners in this enforcement effort. The SEC should consider proposing legislation that allows state regulators to enforce disclosure requirements for exempt offerings. Such a proposal would maintain a uniform set of disclosure rules throughout the states while also allowing for more enforcement resources to ensure compliance with those rules.

[26] *SEC Analysis of Capital Raising in the U.S.*, *supra* note 2, at 7 n.18.

[27] SEC Compliance & Disclosure Interpretation, Question 257.07 (Jan. 26, 2009), https://www.sec.gov/divisions/corpfin/guidance/securitiesactrules-interps.htm.

[28] 17 C.F.R. § 230.507(a). The question arises, however, about the effectiveness of this provision as a deterrent if the issuer fails to file Form D for any subsequent offerings.

untimely Forms D, and there is anecdotal evidence that the SEC most often does nothing about the late filings.[29]

In addition to more proactively enforcing Form D compliance, the SEC should consider reintroducing its 2013 proposed rule change to Rule 507, which would prohibit issuers from using Rule 506 for one year after failing to file a Form D. 78 Fed. Reg. 44,806, 44,817. As the Commission itself acknowledged in that 2013 proposal, Form D's original purpose was to "serve an important data collection function, including, among other things, for the Commission's rulemaking efforts." *Id.* at 44,810. Form D aids state securities regulators as a source of important information when responding to complaints from citizens about unregistered offerings. And it provides at least some data to Congress and outside researchers about one of the most opaque forms of exempt offerings.

2. Reg CF

Reg CF allows issuers to raise up to $1.07 million in capital through online portals without any investor qualification requirements.[30] In exchange for this, issuers must provide disclosures about their business and their financial condition before the offering.[31] Investors, regardless of their income or wealth, are subject to caps on the amount they can invest in Reg CF offerings.[32]

As with the other categories of exempt offerings, the SEC has offered essentially no data on outcomes for investors or issuers in Reg CF offerings. There has been lackluster issuer and investor interest in Reg CF offerings, which may point to a perception that Reg CF offerings do not attract capital. Before making any changes to Reg CF, the SEC should study the outcomes for investors and issuers further.

While undertaking that study, the SEC should maintain requirements by issuers to provide fulsome disclosures to Reg CF investors. Reg CF provides no limitations on the types of investors who can participate in exempt offerings; on paper, crowdfunding operates almost as a small-scale public market. Investor protections are crucial in this kind of setting. Issuer disclosures not only provide individuals with key information

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[29] Jayne E. Juvan, "Missed Form D Filings: Are There Consequences to Operating in Stealth Mode?," *Tucker Ellis LLP Lingua Negoti*, Jan. 25, 2018, https://www.tuckerellis.com/lingua-negoti-blog/missed-form-d-filings-are-there-consequences-to-operating-in-stealth-mode ("Many of the late Form D filings are never addressed by the SEC.").

[30] 17 C.F.R. § 227.100(a)(1).

[31] *See generally* 17 C.F.R. § 227.201.

[32] 17 C.F.R. § 227.100(a)(2).

before they invest, they may also increase investor confidence in the crowdfunding market.[33]

To further ensure protection of investors, the SEC should proactively enforce Reg CF's disclosure requirements. There is data that issuer compliance with Reg CF's disclosure requirements is lackluster. According to a study by University of Mississippi School of Law Professor Mercer Bullard, in the first year of Reg CF, only 56% of Reg CF filers provided all of the Reg CF required financial statements with the correct level of review through either executive certification or independent accountant review.[34] Only 61% of issuers who made successful filings under Reg CF filed the first required annual report.[35] An informal study by our office of more recent compliance with Reg CF's initial disclosures and annual report requirement suggests the trend Professor Bullard identified continues. According to our review of filings between May 1 and August 1, 2019, approximately 40% of Reg CF filers were missing at least one of the financial statement requirements and/or had an incorrect level of review of their financial statements.

There have already been red flags about the conduct of Reg CF issuers and the portals that host them. For example, the Financial Industry Regulatory Authority ("FINRA") recently expelled a crowdfunding portal partially on the basis that the portal ignored warning signs that an issuer was engaged in misleading or fraudulent schemes.[36] In another example, the Investor Advocate raised concerns about the use of Simple Agreements for Future Equity ("SAFEs") by Reg CF issuers.[37] SAFEs, which are "structured to allocate equity to investors when there is a future valuation event," are concerning because they "contain[] certain features that differ from the rights and potential returns that an average equity investor may expect."[38] The pattern of noncompliance with Reg CF's disclosure requirements may provide an environment in which fraud and manipulation flourish.

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[33] Honigsberg, *supra* note 16, at 318-19.

[34] Mercer Bullard, *Crowdfunding's Culture of Noncompliance: An Empirical Analysis* 25 (2019), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3456999.

[35] *Id.* at 45.

[36] *See Dept. of Enf't v. DreamFunded Marketplace LLC*, Disciplinary Proceeding No. 2017053428201, at 111-12 (June 5, 2019).

[37] Office of the Investor Advocate, Sec. & Exch. Comm'n, *Report on Activities, Fiscal Year 2016* 20-21 (2016), https://www.sec.gov/advocate/reportspubs/annual-reports/sec-investor-advocate-report-on-activities-2016.pdf.

[38] *Id.*

Coupled with data that the SEC has engaged in very limited enforcement activity against Reg CF issuers or the portals who host them,[39] this evidence raises concerns about whether investors are actually receiving the protections Reg CF currently mandates. The SEC should engage in meaningful enforcement of the disclosure requirements to incentivize issuers to provide this critical information to investors.

III. CONCLUSION

We appreciate the opportunity to comment on this Concept Release. We encourage the SEC to gather more data and conduct more studies on exempt offerings and how they impact investors and issuers before taking steps to modify the current framework. We hope that the SEC will take our suggestions under consideration as it moves forward.

Sincerely,

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[39] SEC Regulation Crowdfunding Study, p. 42.