

112TH CONGRESS
1ST SESSION

S. 1970

To amend the securities laws to provide for registration exemptions for certain crowdfunded securities, and for other purposes.

IN THE SENATE OF THE UNITED STATES

DECEMBER 8, 2011

Mr. MERKLEY (for himself, Mr. BENNET, and Ms. LANDRIEU) introduced the following bill; which was read twice and referred to the Committee on Banking, Housing, and Urban Affairs

A BILL

To amend the securities laws to provide for registration exemptions for certain crowdfunded securities, and for other purposes.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE.**

4 This Act may be cited as the “Capital Raising Online
5 While Deterring Fraud and Unethical Non-Disclosure Act
6 of 2011” or the “CROWDFUND Act”.

1 **SEC. 2. CROWDFUNDING EXEMPTION.**

2 (a) SECURITIES ACT OF 1933.—Section 4 of the Se-
3 curities Act of 1933 (15 U.S.C. 77d) is amended by add-
4 ing at the end the following:

5 “(6) any transaction involving the offer or sale
6 of securities by an issuer (including all entities con-
7 trolled by or under common control with the issuer),
8 provided that—

9 “(A) the aggregate amount sold to all in-
10 vestors by an issuer, including any amount sold
11 in reliance on the exemption provided under
12 this paragraph during the 12-month period pre-
13 ceeding the date of such transaction, is not more
14 than \$1,000,000, as such amount is adjusted
15 by the Commission by notice published in the
16 Federal Register to reflect the annual change in
17 the Consumer Price Index for All Urban Con-
18 sumers published by the Bureau of Labor Sta-
19 tistics;

20 “(B) the aggregate amount sold to any in-
21 vestor by an issuer, including any amount sold
22 in reliance on the exemption provided under
23 this paragraph during the 12-month period pre-
24 ceeding the date of such transaction, does not
25 exceed the greater of—

1 “(i) \$500, as such amount is adjusted
2 by the Commission by notice published in
3 the Federal Register to reflect the annual
4 change in the Consumer Price Index for
5 All Urban Consumers published by the Bu-
6 reau of Labor Statistics; or

7 “(ii) if the investor has an annual in-
8 come of—

9 “(I) greater than \$50,000 but
10 less than \$100,000 (as such amounts
11 are adjusted by the Commission by
12 notice published in the Federal Reg-
13 ister to reflect the annual change in
14 the Consumer Price Index for All
15 Urban Consumers published by the
16 Bureau of Labor Statistics), 1 percent
17 of the annual income of such investor;
18 or

19 “(II) greater than \$100,000 (as
20 such amount is adjusted by the Com-
21 mission by notice published in the
22 Federal Register to reflect the annual
23 change in the Consumer Price Index
24 for All Urban Consumers published by
25 the Bureau of Labor Statistics), 2

1 percent of the annual income of such
2 investor;

3 “(C) the transaction is conducted through
4 a broker or funding portal that complies with
5 the requirements of section 4A(a); and

6 “(D) the issuer complies with the require-
7 ments of section 4A(b).”.

8 (b) REQUIREMENTS TO QUALIFY FOR
9 CROWDFUNDING EXEMPTION.—The Securities Act of
10 1933 (15 U.S.C. 77a et seq.) is amended by inserting after
11 section 4 the following:

12 **“SEC. 4A. REQUIREMENTS WITH RESPECT TO CERTAIN**
13 **SMALL TRANSACTIONS.**

14 “(a) REQUIREMENTS ON INTERMEDIARIES.—A per-
15 son engaged in the business of effecting transactions in
16 securities for the account of others pursuant to section
17 4(6) shall—

18 “(1) register with the Commission as—

19 “(A) a broker; or

20 “(B) a funding portal (as defined in sec-
21 tion 3(a)(80) of the Securities Exchange Act of
22 1934);

23 “(2) register with any applicable self-regulatory
24 organization (as defined in section 3(a)(26) of the
25 Securities Exchange Act of 1934);

1 “(3) provide such disclosures, including disclo-
2 sures related to risks and other investor education
3 materials, as the Commission shall, by rule, deter-
4 mine appropriate;

5 “(4) ensure that each potential investor—

6 “(A) reviews investor-education informa-
7 tion, in line with standards established by the
8 Commission, by rule;

9 “(B) positively affirms that the investor
10 understands that the investor is risking the loss
11 of the entire investment, and that the investor
12 could bear such a loss; and

13 “(C) answers questions demonstrating—

14 “(i) an understanding of the level of
15 risk generally applicable to investments in
16 startups, emerging businesses, and small
17 issuers;

18 “(ii) an understanding of the risk of
19 illiquidity; and

20 “(iii) an understanding of such other
21 matters as the Commission determines ap-
22 propriate, by rule;

23 “(5) take such measures to reduce the risk of
24 fraud with respect to such transactions, as estab-
25 lished by rule of the Commission, including obtain-

1 ing a criminal background check and securities en-
2 forcement regulatory history check on each officer,
3 director, and person holding more than 20 percent
4 of the shares of every issuer whose securities are of-
5 fered by such person;

6 “(6) not later than 1 month prior to the first
7 day on which securities are offered to any potential
8 investor (or such other period as the Commission
9 may establish), provide in writing to the Commission
10 and each potential investor any information provided
11 by the issuer pursuant to subsection (b);

12 “(7) ensure that all offering proceeds are only
13 provided to the issuer when the aggregate capital
14 raised from all investors is equal to the target offer-
15 ing amount, and allow all investors to cancel their
16 commitments to invest, as the Commission, by rule,
17 shall determine appropriate;

18 “(8) make such efforts as the Commission de-
19 termines appropriate, by rule, to ensure that, for
20 any offering made pursuant to section 4(6), that no
21 investor exceeds the investment limits set forth in
22 section 4(6)(B);

23 “(9) make such efforts as the Commission de-
24 termines appropriate, by rule, to ensure that no in-
25 vestor has purchased securities offered pursuant to

1 section 4(6), that in the aggregate from all issuers,
2 exceed the greater of—

3 “(A) \$2,000 (as such amount is adjusted
4 by the Commission, by notice published in the
5 Federal Register to reflect the annual change in
6 the Consumer Price Index for All Urban Con-
7 sumers published by the Bureau of Labor Sta-
8 tistics); or

9 “(B) if the investor has an annual income
10 of—

11 “(i) greater than \$50,000 but not
12 more than \$100,000 (as such amounts are
13 adjusted by the Commission, by notice
14 published in the Federal Register to reflect
15 the annual change in the Consumer Price
16 Index for All Urban Consumers published
17 by the Bureau of Labor Statistics), 4 per-
18 cent of the annual income of such investor;
19 or

20 “(ii) greater than \$100,000 (as such
21 amount is adjusted by the Commission by
22 notice published in the Federal Register to
23 reflect the annual change in the Consumer
24 Price Index for All Urban Consumers pub-
25 lished by the Bureau of Labor Statistics),

1 8 percent of the annual income of such in-
2 vestor;

3 “(10) takes such steps to protect the privacy of
4 information collected from investors as the Commis-
5 sion shall, by rule, determine appropriate;

6 “(11) not compensate promoters, finders, lead
7 generators, or other persons to attract or provide the
8 personal information of any potential investor;

9 “(12) prohibit its directors, officers, partners,
10 or employees (or any person occupying a similar sta-
11 tus or performing a similar function) from having
12 any financial interest in an issuer using its services;
13 and

14 “(13) meet such other requirements as the
15 Commission may, by rule, prescribe.

16 “(b) REQUIREMENTS FOR ISSUERS.—For purposes
17 of section 4(6), an issuer who offers or sells securities
18 shall—

19 “(1) be organized under and subject to the laws
20 of a State;

21 “(2) file with the Commission and provide to
22 actual and potential investors and the relevant
23 broker or funding portal—

24 “(A) the name, legal status, physical ad-
25 dress, and website address of the issuer;

1 “(B) the names of the directors and offi-
2 cers (and any persons occupying a similar sta-
3 tus or performing a similar function), and each
4 person holding more than 20 percent of the
5 shares of the issuer;

6 “(C) a description of the business of the
7 issuer and the anticipated business plan of the
8 issuer;

9 “(D) a description of the financial condi-
10 tion of the issuer, including—

11 “(i) financial statements reviewed by
12 a public accountant who is independent of
13 the issuer, using professional standards
14 and procedures for such review or stand-
15 ards and procedures established by rule of
16 the Commission for such purpose; or

17 “(ii) for offerings seeking to raise
18 more than \$500,000 (or such other
19 amount as may be established by the Com-
20 mission, by rule), audited financial state-
21 ments;

22 “(E) a description of the stated purpose
23 and intended use of the proceeds of the offering
24 sought by the issuer;

1 “(F) the target offering amount, the dead-
2 line to reach the target offering amount, and
3 regular updates regarding the progress of the
4 issuer in meeting the target offering amount;

5 “(G) the price at which the securities will
6 be offered for a given ownership stake;

7 “(H) a description of the ownership and
8 capital structure of the issuer, how the securi-
9 ties being offered are being valued, what the
10 rights of the securities are, and how rights may
11 be exercised by the issuer and shareholders; and

12 “(I) such other information as the Com-
13 mission may, by rule, prescribe;

14 “(3) not advertise the specific details of the of-
15 fering, except for notices which direct investors to
16 the funding portal or broker;

17 “(4) file with the Commission and provide to
18 investors quarterly reports of the results of oper-
19 ations and financial statements, as the Commission
20 shall, by rule, determine appropriate, subject to such
21 exceptions and termination dates as the Commission
22 may establish, by rule; and

23 “(5) comply with such other requirements as
24 the Commission may prescribe, by rule.

1 “(c) LIABILITY FOR MISSTATEMENTS.—The issuer
2 and any person who is a director or officer (or any person
3 occupying a similar status or performing a similar func-
4 tion) or partner in the issuer shall be liable to any person
5 acquiring such security that was subject to an offering
6 pursuant to section 4(6) for any untrue statement of a
7 material fact or omission to state a material fact required
8 to be stated in connection with any offering made pursu-
9 ant to section 4(6).

10 “(d) INFORMATION AVAILABLE TO STATES.—The
11 Commission shall make the information described in sub-
12 section (b) and such other information as the Commission,
13 by rule, determines appropriate, available to the appro-
14 priate securities regulatory authority of each State.

15 “(e) RESTRICTIONS ON SALES.—Securities issued
16 pursuant to a transaction described in section 4(6)—

17 “(1) may not be transferred by the purchaser
18 of such securities during the 2-year period beginning
19 on the date of purchase, unless such securities are
20 transferred—

21 “(A) to the issuer of the securities;

22 “(B) to an accredited investor;

23 “(C) as part of an offering registered with
24 the Commission; or

1 “(D) to a member of the family of the pur-
2 chaser or the equivalent, or in connection with
3 the death of the purchaser; and

4 “(2) shall be subject to such other limitations
5 as the Commission shall establish, by rule.

6 “(f) RULE OF CONSTRUCTION.—Nothing in this sec-
7 tion or section 4(6) shall be construed as preventing an
8 issuer from raising capital through methods not described
9 under section 4(6).”.

10 (c) RULEMAKING.—Not later than 1 year after the
11 date of enactment of this Act, the Securities and Ex-
12 change Commission (in this Act referred to as the “Com-
13 mission”) shall issue such rules as may be necessary to
14 carry out section 4(6) and section 4A of the Securities
15 Act of 1933, as added by this Act.

16 (d) DISQUALIFICATION.—Not later than 1 year after
17 the date of enactment of this Act, the Commission shall,
18 by rule, establish disqualification provisions that are sub-
19 stantially similar to the disqualification provisions con-
20 tained in the regulations adopted in accordance with sec-
21 tion 926 of the Dodd-Frank Wall Street Reform and Con-
22 sumer Protection Act (15 U.S.C. 77d note)—

23 (1) under which an issuer shall not be eligible
24 to offer securities pursuant to section 4(6) of the Se-
25 curities Act of 1933, as added by this Act; and

1 (2) under which a funding portal or broker
 2 shall not be eligible to effect transactions for the ac-
 3 count of others pursuant to section 4(6) of the Secu-
 4 rities Act of 1933, as added by this Act.

5 **SEC. 3. EXCLUSION OF CROWDFUNDING INVESTORS FROM**
 6 **SHAREHOLDER CAP.**

7 Section 12(g) of the Securities Exchange Act of 1934
 8 (15 U.S.C. 78l(g)) is amended by adding at the end the
 9 following:

10 “(6) EXCLUSION FOR PERSONS HOLDING CER-
 11 TAIN SECURITIES.—The Commission may, as appro-
 12 priate, exempt from this subsection securities ac-
 13 quired pursuant to an offering made under section
 14 4(6) of the Securities Act of 1933.”.

15 **SEC. 4. FUNDING PORTAL REGULATION.**

16 (a) EXEMPTION.—

17 (1) IN GENERAL.—Section 3 of the Securities
 18 Exchange Act of 1934 (15 U.S.C. 78c) is amended
 19 by adding at the end the following:

20 “(h) LIMITED EXEMPTION FOR FUNDING POR-
 21 TALS.—The Commission shall, by rule, as the Commission
 22 determines appropriate, exempt funding portals from the
 23 registration requirements of section 15(a)(1), condi-
 24 tionally or unconditionally, provided that such funding
 25 portals remain subject to such examination by the Com-

1 mission and a national securities association and to such
2 other requirements under this title as the Commission de-
3 termines appropriate under such rule.”.

4 (2) RULEMAKING.—A rule to carry out section
5 3(h) of the Securities Exchange Act of 1934 (15
6 U.S.C. 78c), as added by this subsection, shall be
7 issued not later than 1 year after the date of enact-
8 ment of this Act.

9 (b) DEFINITION.—Section 3(a) of the Securities Ex-
10 change Act of 1934 (15 U.S.C. 78c(a)) is amended by
11 adding at the end the following:

12 “(80) FUNDING PORTAL.—The term ‘funding
13 portal’ means any person engaged in the business of
14 effecting transactions in securities for the account of
15 others, solely pursuant to section 4(6) of the Securi-
16 ties Act of 1933 (15 U.S.C. 77d(6)) that does not—

17 “(A) offer investment advice or rec-
18 ommendations;

19 “(B) solicit purchases, sales, or offers to
20 buy the securities offered or displayed on its
21 website or portal;

22 “(C) compensate employees, agents, or
23 other third parties for such solicitation or based
24 on the sale of securities displayed or references
25 on its website or portal;

1 “(D) hold, manage, possess, or otherwise
2 handle investor funds or securities; or

3 “(E) engage in such other activities as the
4 Commission may, by rule, determine appro-
5 priate.”.

6 **SEC. 5. FRAUD RESPONSE REVIEW.**

7 The Commission shall conduct a review of the effects
8 of the provisions of this Act on investor protection—

9 (1) once every 6 months during the first 2
10 years after the date of enactment of this Act;

11 (2) annually during the 3 years following the 2-
12 year period referred to in paragraph (1); and

13 (3) not less frequently than once every 5 years
14 thereafter.

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