

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.

○