March 7, 2012

The Honorable Harry Reid

Majority Leader

U. S. Senate

S-221, The Capitol

Washington, DC 20510

RE: Investor Protection, Market Integrity and Small Business Capital Formation

Dear Leader Reid:

On behalf of AARP, I am writing to express concern with respect to a package of "capital formation" bills that have been approved by the House of Representatives as well as related Senate companion measures we understand soon will be considered on the Senate floor. AARP's primary concern is that these bills, advanced based on their potential to help create jobs, inadequately protect against the potential harmful impact on investor protections and market integrity.

The goal of facilitating access to capital for new and small businesses as a means of promoting job growth is a worthy one. We agree that removing regulatory impediments that undermine

capital formation are warranted. However, we do not agree that the best way to create jobs is to weaken essential regulatory protections that were put in place to address specific problems that would otherwise still exist. Our view is that the Senate now has the opportunity to take a more balanced approach, recognizing both an interest in facilitating access to capital for new and small business and in preserving essential regulations that protect investors from fraud and abuse, promote the transparency on which well-functioning markets depend, and ensure a fair and efficient marketplace.

This debate is critical to older investors, who with a lifetime of savings and investments, are disproportionately represented among the victims of securities fraud. We share the concerns expressed by the North American Securities Administrators (NASAA) and others who testified before the Senate Banking Committee that absent proper oversight and investor protections, the capital formation proposals now under consideration very well may, in varying degrees, open the floodgates to a repeat of the kind of penny stock and other "boiler room" frauds that have ensnared financially unsophisticated and vulnerable investors in the past. The absence of adequate regulation has been shown to have undermined the integrity of the markets and damaged investor confidence while having no positive impact on the creation of new jobs, the stated purpose of the legislation in question.

While each of the bills in the package presents its own investor protection concerns, AARP's primary interest is in H.R. 2940/S. 1831, the "Access to Capital for Job Creators Act," and H.R. 2930/S. 1970/S. 1791, the "Democratizing Access to Capital Act."

Regulation D Revisions (H.R. 2940, S. 1831)

This legislation would lift the Regulation D ban on public solicitation of accredited investors in unregistered securities, despite the fact that these offerings have become a source of significant market abuses, according to the North American Securities Administrators Association (NASAA) and other experts. Regulation D investments are considered riskier than regular stocks because they do not face the same regulatory scrutiny. Brokers are supposed to sell them only to so-called accredited investors, such as wealthy individuals and large institutions. However, the definition of accredited investor has changed little since it was first introduced by the Securities and Exchange Commission (SEC) more than three decades ago, and includes many individuals who do not always have the necessary financial expertise to evaluate the risks inherent in these investments. This situation has been exploited by unscrupulous operators who sell risky products to unsophisticated investors, particularly retirees. As one expert in state regulatory cases noted, "We are seeing private placements being sold to retail investors that barely meet the standard that was set in 1982. Oftentimes, the investors are retired, not financially savvy and are solicited

by brokers." If limitations on general solicitation are eliminated, such individuals soon could be flooded with such high risk and dubious "opportunities."

The concept of this legislation is not a new one; in 1992, the SEC rewrote the regulations to allow for general solicitation in private offerings as suggested in the pending legislation. In 1999, the SEC restored the advertising restrictions based on "investor protection concerns" that "require that this action be taken to curb misuse of this exemption in the markets for microcap companies." In 2007, the SEC again considered and rejected implementing this rule change.

While the existing rules regarding general solicitation may merit review, this legislation represents a very considerable redrawing of the lines between public and private markets, and should not be enacted without greater attention to the potential risks of such an approach. We urge the Senate to conduct further study in order to determine whether legislation is needed and, if so, to adopt a much more narrowly targeted approach.

Crowd-Funding (H.R. 2930/S. 1970/S. 1791)

These bills would create a "crowd-funding" exemption from federal and state securities laws, allowing speculative start-up ventures to advertise publicly on the Internet and raise money from an unlimited number of shareholders.

Even the best of the crowd-funding bills would make it possible for the least sophisticated investors to risk their limited funds investing in the most speculative small companies. These investments would be made without the opportunity for extensive due diligence that venture capital funds and angel investors engage in before making comparable investments. That may be why Columbia Law School professor Jack Coffee testified before the Senate Banking Committee that H.R. 2930 should be re-titled "the Boiler Room Preservation Act."

At best, even if Congress does everything right in terms of imposing appropriate investor protections, most of those who invest through crowd-funding sites are likely to lose some or all of their money. At worst, crowd-funding web sites could become the new turbo-charged pump-and-dump boiler room operations of the internet age. Meanwhile, money that could have been invested in small companies with real potential for growth would be syphoned off into these financially shakier, more speculative ventures. The net effect would likely be to undermine

rather than support sustainable job growth. For that reason, we question the wisdom of adopting any of the proposed crowd-funding bills.

Among the various bills, however, S. 1970 stands out as a serious and responsible effort to ensure that crowd-funding sites are appropriately regulated. In particular, we appreciate S. 1970's inclusion of an aggregate cap on investments, its requirement that crowd-funding sites be registered with and subject to regulatory oversight by the SEC, its more robust requirements regarding the duties of those intermediaries to prevent fraud, its prohibition against active solicitation by sites that are not registered as a broker-dealer, and its preservation of state authority. If Congress moves forward with this type of legislation, it should at least adopt the more robust investor protections in S. 1970 to minimize the potential harm to unwary investors and to maximize the potential that investments through these sites support legitimate businesses.

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As the Senate moves forward on these proposals, we urge you to insist that any legislation intended to promote capital formation protects investors, promotes transparency, and ensures the integrity and stability of the financial marketplace. Investors still reeling from the most recent financial crisis deserve no less.

If you have any further questions, please feel free to contact me, or have your staff contact Mary Wallace of our Government Affairs staff at 202-434-3954.

Sincerely,

Joyce A. Rogers

Senior Vice President

Government Affairs

cc: Banking Committee Chairman Tim Johnson

Banking Committee Ranking Member Richard Shelby

Members, Banking Committee