

**EMPOWERING ENTREPRENEURS:  
REMOVING BARRIERS TO CAPITAL  
ACCESS FOR SMALL BUSINESSES**

---

---

**HEARING**  
BEFORE THE  
SUBCOMMITTEE ON CAPITAL MARKETS  
OF THE  
COMMITTEE ON FINANCIAL SERVICES  
U.S. HOUSE OF REPRESENTATIVES  
ONE HUNDRED EIGHTEENTH CONGRESS  
FIRST SESSION

—————  
FEBRUARY 8, 2023  
—————

Printed for the use of the Committee on Financial Services

**Serial No. 118-4**



—————  
U.S. GOVERNMENT PUBLISHING OFFICE

52-359 PDF

WASHINGTON : 2023

HOUSE COMMITTEE ON FINANCIAL SERVICES

PATRICK MCHENRY, North Carolina, *Chairman*

FRANK D. LUCAS, Oklahoma	MAXINE WATERS, California, <i>Ranking</i>
PETE SESSIONS, Texas	<i>Member</i>
BILL POSEY, Florida	NYDIA M. VELÁZQUEZ, New York
BLAINE LUETKEMEYER, Missouri	BRAD SHERMAN, California
BILL HUIZENGA, Michigan	GREGORY W. MEEKS, New York
ANN WAGNER, Missouri	DAVID SCOTT, Georgia
ANDY BARR, Kentucky	STEPHEN F. LYNCH, Massachusetts
ROGER WILLIAMS, Texas	AL GREEN, Texas
FRENCH HILL, Arkansas	EMANUEL CLEAVER, Missouri
TOM EMMER, Minnesota	JIM A. HIMES, Connecticut
BARRY LOUDERMILK, Georgia	BILL FOSTER, Illinois
ALEXANDER X. MOONEY, West Virginia	JOYCE BEATTY, Ohio
WARREN DAVIDSON, Ohio	JUAN VARGAS, California
JOHN ROSE, Tennessee	JOSH GOTTHEIMER, New Jersey
BRYAN STEIL, Wisconsin	VICENTE GONZALEZ, Texas
WILLIAM TIMMONS, South Carolina	SEAN CASTEN, Illinois
RALPH NORMAN, South Carolina	AYANNA PRESSLEY, Massachusetts
DAN MEUSER, Pennsylvania	STEVEN HORSFORD, Nevada
SCOTT FITZGERALD, Wisconsin	RASHIDA TLAIB, Michigan
ANDREW GARBARINO, New York	RITCHIE TORRES, New York
YOUNG KIM, California	SYLVIA GARCIA, Texas
BYRON DONALDS, Florida	NIKEMA WILLIAMS, Georgia
MIKE FLOOD, Nebraska	WILEY NICKEL, North Carolina
MIKE LAWLER, New York	BRITTANY PETTERSEN, Colorado
ZACH NUNN, Iowa	
MONICA DE LA CRUZ, Texas	
ERIN HOUCHIN, Indiana	
ANDY OGLES, Tennessee	

MATT HOFFMANN, *Staff Director*

SUBCOMMITTEE ON CAPITAL MARKETS

ANN WAGNER, Missouri, *Chairwoman*

FRANK D. LUCAS, Oklahoma  
PETE SESSIONS, Texas  
BILL HUIZENGA, Michigan  
FRENCH HILL, Arkansas  
TOM EMMER, Minnesota  
ALEXANDER X. MOONEY, West Virginia  
BRYAN STELL, Wisconsin  
DAN MEUSER, Pennsylvania  
ANDREW GARBARINO, New York, *Vice  
Chairman*  
MIKE LAWLER, New York  
ZACH NUNN, Iowa  
ERIN HOUCIN, Indiana

BRAD SHERMAN, California, *Ranking  
Member*  
GREGORY W. MEEKS, New York  
DAVID SCOTT, Georgia  
JUAN VARGAS, California  
JOSH GOTTHEIMER, New Jersey  
VICENTE GONZALEZ, Texas  
SEAN CASTEN, Illinois  
WILEY NICKEL, North Carolina  
STEPHEN F. LYNCH, Massachusetts  
EMANUEL CLEAVER, Missouri



# CONTENTS

---

	Page
Hearing held on:	
February 8, 2023 .....	1
Appendix:	
February 8, 2023 .....	35

## WITNESSES

WEDNESDAY, FEBRUARY 8, 2023

Conwell, McKeever E. II, Founder and Managing Partner, RareBreed Ventures .....	5
Ellenoff, Douglas, Partner, Ellenoff Grossman & Schole LLP .....	6
Gladney, Deborah, CEO and Co-Founder, WorkTorch .....	8
Howe, Darcy A., Founder and Managing Director, KCRise Fund .....	10
Thornton, Alexandra, Senior Director, Center for American Progress .....	11

## APPENDIX

Prepared statements:	
Conwell, McKeever E. II .....	36
Ellenoff, Douglas .....	41
Gladney, Deborah .....	49
Howe, Darcy A. ....	51
Thornton, Alexandra .....	53

## ADDITIONAL MATERIAL SUBMITTED FOR THE RECORD

Wagner, Hon. Ann:	
Written responses to questions for the record submitted to Deborah Gladney .....	60
Garbarino, Hon. Andrew:	
Written statement of the National Venture Capital Association (NVCA) ...	61
Written statement of the Small Business Investor Alliance (SBIA) .....	63
Houchin, Hon. Erin:	
Written responses to questions for the record submitted to McKeever E. Conwell II .....	65
Lawler, Hon. Mike:	
Written responses to questions for the record submitted to Deborah Gladney .....	70
Meuser, Hon. Dan:	
Written statement of the Center for American Entrepreneurship .....	72
Written statement of the U.S. Chamber of Commerce .....	74
Waters, Hon. Maxine:	
“An Iowa Farmer Tried to Dodge Stock-Market Turmoil. It Cost Him \$900,000.”, dated January 13, 2023 .....	78
North American Securities Administrators Association (NASAA) Report and Recommendations for Reinvigorating Our Capital Markets,” dated February 7, 2023 .....	84
Written statement of Public Citizen .....	138
Ellenoff, Douglas:	
U.S. Securities and Exchange Commission’s Office of the Advocate for Small Business Capital Formation’s Annual Report Fiscal Year 2022 ....	143



**EMPOWERING ENTREPRENEURS:  
REMOVING BARRIERS TO CAPITAL  
ACCESS FOR SMALL BUSINESSES**

---

**Wednesday, February 8, 2023**

U.S. HOUSE OF REPRESENTATIVES,  
SUBCOMMITTEE ON CAPITAL MARKETS,  
COMMITTEE ON FINANCIAL SERVICES,  
*Washington, D.C.*

The subcommittee met, pursuant to notice, at 2:05 p.m., in room 2128, Rayburn House Office Building, Hon. Ann Wagner [chairwoman of the subcommittee] presiding.

Members present: Representatives Wagner, Lucas, Sessions, Huizenga, Hill, Emmer, Mooney, Meuser, Garbarino, Lawler, Nunn, Houchin; Sherman, Vargas, Gottheimer, Casten, Nickel, Lynch, and Cleaver.

Ex officio present: Representative Waters.

Chairwoman WAGNER. The Subcommittee on Capital Markets will come to order.

Without objection, the Chair is authorized to declare a recess of the subcommittee at any time.

Today's hearing is entitled, "Empowering Entrepreneurs: Removing Barriers to Capital Access for Small Businesses."

I now recognize myself for opening remarks.

Eleven years ago, the Jumpstart Our Business Startups (JOBS) Act of 2012 was enacted into law by a divided Congress, with the intention of increasing access to capital for small businesses and entrepreneurs in the United States. The purpose of the JOBS Act was to provide greater opportunities for small business owners and entrepreneurs to grow their companies and create jobs in their communities.

Despite the successes of the JOBS Act, there are still significant regulatory barriers that impede the growth of small businesses and hinder the competitiveness of job growth in the United States. Small businesses, which make up 99 percent of all enterprises and employ almost half of the U.S. workforce, are disproportionately affected by these barriers. The lack of access to capital makes it challenging for small business owners to grow and expand their companies, which can limit job creation and, of course, economic growth.

For this reason, I am thrilled to convene this hearing today and to discuss policy reforms that will reduce the obstacles and improve access to capital for small and private businesses and entrepreneurs across the country, not just in the financial centers on our nation's coasts but in every State.

The decline in small business loan approval rates from 81 percent before the COVID-19 pandemic to 68 percent in 2021 underscores the importance of maintaining and enhancing our private markets as a viable option for small business capital needs.

If we limit access to capital in our private markets, as SEC Chair Gensler intends to do, where will small businesses turn for funding, considering the decrease, in particular, in loan approval rates? The need for access to capital is critical, and small businesses must have options available to them to secure the funding they need to grow and create jobs.

Republicans on this committee believe that entrepreneurs and founders should raise money with as little friction as possible. As a result, Congress and regulators must adopt common-sense, forward-thinking policies that reduce barriers and increase access to capital, raising opportunities for American entrepreneurs.

The proposed legislation that we are discussing today will lead to increased competitiveness and more opportunities for companies on Main Street to thrive. Healthy public and private markets can coexist, and we should work together to pursue policies that make both markets attractive places to raise capital and spur economic growth.

As the Chair of this subcommittee, I am eager to tackle these regulatory barriers that prevent small businesses and entrepreneurs from accessing capital. Today's proposals will enable all entrepreneurs, including those who have been overlooked and underserved, to create jobs and grow their businesses, regardless of their background or location. Our goal is to ensure that small business owners and entrepreneurs have the resources they need to succeed and create jobs in their communities.

In conclusion, the JOBS Act of 2012 was a step in the right direction, but there is still much work to be done to improve access to capital for small businesses and entrepreneurs. The regulatory barriers that exist must be addressed and policy reforms must be implemented to reduce these obstacles and enhance access to capital. This will enable small businesses to grow and create jobs, contributing to the overall economic growth and competitiveness of the United States.

I am committed to working with my colleagues in this subcommittee to achieve these goals and to make the American Dream a reality for entrepreneurs.

The Chair now recognizes the ranking member of the subcommittee, Mr. Sherman, for 5 minutes for an opening statement.

Mr. SHERMAN. I'm glad we are having this hearing, our second hearing today. I am a little jealous of Chairwoman Wagner, for she is in a situation where she is allowed to hold two hearings in one day. Sometimes, you are not allowed to hold two hearings in the same month, under some circumstances.

We are talking about removing barriers to private placements and small businesses. Keep in mind that sometimes barriers are good, and sometimes they are not. We are always told the barrier prevented you from investing in Apple. Maybe it prevented you from investing in Pear, Banana, or Kumquat.

And when a barrier successfully prevents an investor from investing in a bad or fraudulent investment or an investment where

there is not enough information to evaluate it, that is not just good for that one investor, it is good for our overall capital markets. The willingness of Americans to invest is dependent upon the protections they enjoy.

And our present system is not working all that poorly when the private placement market raised \$4.45 trillion from July 1, 2021, to June 30, 2022, and it did so without the biggest frauds and disasters that we are aware of coming to mind. I remember when the biggest failures were WorldCom and Enron. Today, the biggest failures or most famous ones that come to mind are FTX and Luckin Coffee, not subject to U.S. regulation. If you send your money to China, or you send your money to the Bahamas, you cannot then complain that Gary Gensler did not protect you.

We should be drafting statutes that help genuinely small businesses. When people in my district think of small businesses, they think of Casa Vega on Ventura Boulevard, not some company with a \$2-billion capitalization. That doesn't mean we shouldn't draft statutes that help medium-size businesses, but we shouldn't paint a picture of a pizzeria and then draft a bill for a \$2 billion enterprise. We need the right picture when we are drafting the bill.

As I think all of you know, I am old. Even before I came to Congress, I was in the business world as a CPA and attorney. And back then, banks lent money to small businesses even when there was a chance of failure and without taking a note on the owner's home. They would make a prime plus 3, a prime plus 4, or a prime plus 5 loan, and that was a fair loan because that loan had a 4 or 5 percent chance of a default. The business might have a 4 to 5 percent chance of failing. And if that were to happen, the bank might recoup only half of the money that it lent.

Today's bank examiners won't let you do that, so banks, the traditional way a small business gets financed, aren't available. I made that point in this room, not at our hearing but at our Financial Institutions and Monetary Policy Subcommittee hearing this morning. What we need is for our banks to be able to have a portion of their loans, a portfolio with some risk of default and some risk of loss.

A second source of capital is a small business investment company. Last year, along with Mr. Huizenga, I introduced a bill that would help those companies get capital and then put their capital into small businesses. Due to a quirk, investment index mutual funds can't really invest in business development companies (BDCs) because of the way the SEC defines the expenses of the mutual fund that is making the investment.

BDCs are a vital source of capital to the genuinely small business. We are going to reintroduce this legislation. We are looking for cosponsors who want to be originals. We will probably reintroduce it tomorrow. It is the Access to Small Business Investor Capital Act.

I am told that between the two hearings today, and the one we will do in early March, that we will be considering 30 bills, including discussion drafts. As far as I know, the Access to Small Business Investor Capital Act will be the only one that has an official Democratic chief author, although I am thrilled to have Mr. Huizenga working with me on the bill. And I am hoping that we

won't just be talking about 30 bills, but even more with Democratic chief authors.

I look forward to working with you both in the morning and the afternoon to have a balanced approach to making more rational our private offerings, not with the goal of reducing or increasing regulation, but making it more rational.

I yield back.

Chairwoman WAGNER. Thank you, Ranking Member Sherman.

We have offered, after the notification of this hearing, bills to be put forward for consideration. I am sure there will be a lot of Democrat co-leads on many of our bills. So, we look forward to working together. And I promise I will make you work morning and afternoon, but rarely nights. So, here we are.

I want to welcome our witnesses. First, we are going to hear from Mr. Mac Conwell. Mr. Conwell is the founder and managing partner of RareBreed Ventures, an emerging venture capital (VC) fund located in Baltimore, Maryland. Mr. Conwell is a former software engineer and two-time founder. When he started his first fund, he did not have a network of limited partners, so he raised money on Twitter under the Rule 506(c) reforms implemented by the JOBS Act of 2012. Welcome.

Second, Mr. Doug Ellenoff—a regular here, I believe—is a partner with Ellenoff Grossman & Schole LLP. His practice focuses mostly on business transactions, mergers and acquisitions, and corporate financings. During his career, he has represented numerous broker-dealers, venture capital investor groups, and many corporations involved in the capital formation process. Welcome.

Third, Ms. Deborah Gladney is the CEO and is co-founder of WorkTorch. Ms. Gladney is an entrepreneur with more than a decade of experience designing communication strategies and programs. Prior to co-founding WorkTorch, an education tech company in Wichita, Kansas, she managed stakeholder engagement, media relations, reputation management, and strategic positioning for corporations and nonprofit organizations. Welcome.

Fourth, Ms. Darcy Howe—who now hails from Kansas City, Missouri, but she used to be a constituent of mine in Kirkwood, Missouri—is the founder and managing director of the KCRise Fund. Ms. Howe has been an angel investor for 20 years. She is a founding member of a private banking and investment group of Merrill Lynch in Kansas City, which grew from 30 advisers to 350, with \$240 billion in assets under management and over \$1 billion in revenue before her retirement in 2015. She started KCRise Fund after recognizing the need for local economic growth in middle-income areas in the greater Kansas City region. Welcome.

And finally, Ms. Alexandra Thornton is the senior director of Tax Policy with the Center for American Progress. Prior to joining the Center for American Progress, she worked as the executive vice president for policy, planning, and business affairs at the Jane Goodall Institute, and was a tax policy adviser to a U.S. Senator who served on the Senate Finance Committee, where she provided counsel on trade, banking, and securities issues.

I want to thank all of you for taking the time to be here. Each of you will be recognized for 5 minutes to give an oral presentation

of your testimony. We are going to have a tight gavel here today, so pay attention to the clock, please.

And without objection, each of your written statements will be made a part of the record.

Mr. Conwell, you are now recognized for 5 minutes for your oral testimony.

**STATEMENT OF MCKEEVER E. CONWELL II, FOUNDER AND  
MANAGING PARTNER, RAREBREED VENTURES**

Mr. CONWELL. Thank you. Chairwoman Wagner, Ranking Member Sherman, and members of the subcommittee, thank you for the opportunity to testify today on the importance of creating better access to capital for both entrepreneurs and those who fund their amazing companies.

My name is McKeever Edward Conwell II, and I am the founder and managing partner of RareBreed Ventures, or RareBreed, which I am representing today. RareBreed is a venture capital, or VC, firm that invests in and supports innovative startups in the earliest stages.

I want to first say that I am here to address the much-needed Improving Capital Allocation for Newcomers (ICAN) Act, due to my personal experience in raising a fund and my expertise, but I am in full support of all seven bills being addressed today.

In 2020, I launched RareBreed Ventures as a response to the lack of access to capital for founders of color and founders outside of major investment hubs, as well as a response to a lack of cultural competency from many VCs when it came to investing in founders who didn't look like them or didn't come from similar backgrounds.

These two issues came to me in the form of Shawna Stepp-Jones, a Black single mother from Baltimore who was creating a dryer for wigs. I immediately got what she was creating, but other investors didn't. So after 3 years of getting noes from folks who didn't look like her, she decided the only way for her to get access to capital was to become a surrogate mother, even knowing that Black women are 3 times more likely to die from pregnancy-related causes.

This is why I started RareBreed Ventures, but I didn't have a network of wealthy folks to raise the funds from, so it forced me to get creative and use two regulations to help. The first was Rule 506(c) of Regulation D, which allows for public solicitation of a fund's offering, but requires that every investor in that fund be an accredited investor. And the second was an amendment to Section 3(c)(1) of the Investment Company Act of 1940, which allows a fund of \$10 million or less to have up to 250 investors instead of 100.

The first regulation allowed me to use social media, Twitter mainly, to meet with many potential investors. Thanks to this, I was able to have 1,128 meetings in my first 90 days and more than 4,000 meetings in total. The second regulation allowed me to offer investors to invest as little as \$10,000, compared to the \$100,000 I would have had to ask them to invest before the amendment.

This led to me having 194 investors in RareBreed. Of these investors, 83.5 percent invested \$50,000 or less. Many of these investors are people of color and/or first-time investors in a fund, be-

cause they hadn't had access to make such an investment or couldn't risk the high minimum threshold for funds. This means that before, they were limited to investing in companies either directly, where there is a much higher risk of them losing all of their money, or investing in stocks of publicly-traded companies, which the average venture fund has historically outperformed, according to the Harvard Business Review.

But unfortunately, without the ICAN Act, almost all of these small-dollar investors, who make up 83 percent of our investors, will not be able to invest in RareBreed Ventures Fund II, that is 162 out of 194 investors, since our new minimum will have to be at \$250,000 or more.

The current rules limit the amount of capital and sources of capital for small and new investment funds, leading to less capital to help drive innovation, economic growth, and job creation, especially when we are talking about companies started by founders of color, because we know that, in particular, Black-led funds are 4 times more likely to invest in Black-led companies. Also, keeping in mind that almost all of the Black-led venture funds in America would fit under the new rules of the ICAN Act, because most of us have funds that are less than \$150 million.

With the ICAN Act, such limiting factors would be greatly reduced, allowing more accredited investors to have opportunities to participate in the asset class. With lower minimums, investors can potentially invest smaller amounts of money into more VC funds to spread out their risk and better diversify their investments.

Today, many funds have to turn away investors because of these current limits. This results in the loss of millions of dollars in potential funding for future innovation and job creation, while also excluding investors from being able to truly diversify their own investments and limiting their ability to wealth creation.

Even more so, those who do have enough wealth to continue to participate in the venture asset class are almost exclusively from a non-diverse population. This only serves to further widen the racial and gender wealth gap here in America and puts limits on the types of innovation we see in this country.

In conclusion, I am excited to see Congress working through issues that impact access to capital and drive innovation. As someone who has spent my entire career in venture capital as an advocate for access to capital and reducing barriers, I look forward to supporting and assisting this committee in any way possible.

Thank you for the opportunity to testify today, and I look forward to your questions.

[The prepared statement of Mr. Conwell can be found on page 36 of the appendix.]

Chairwoman WAGNER. And we thank you.

Mr. Ellenoff, you are now recognized for 5 minutes to give your oral testimony.

**STATEMENT OF DOUGLAS ELLENOFF, PARTNER, ELLENOFF  
GROSSMAN & SCHOLE LLP**

Mr. ELLENOFF. Good afternoon, Chairwoman Wagner, Ranking Members Sherman and Waters, and members of the Capital Mar-

kets Subcommittee. It is a pleasure to be a part of this important hearing.

I was last here in front of this subcommittee on September 11, 2019, for the hearing examining private market exemptions as a barrier to IPOs and retail investment. There have been significant developments in the capital market since, and we are now back to an environment where entrepreneurs need further assistance from Congress. I trust that you will seriously consider the proposed bills, all of which I support.

My name is Doug Ellenoff. I am a partner in the New York-based law firm of Ellenoff Grossman & Schole. I am a corporate and securities lawyer and have been practicing for over 35 years. My law firm has been in business for more than 30 years, has nearly 130 lawyers, and we are regularly one of the top 10 IPO law firms in the country, and we do an equal number of other types of financings. We are market leaders in several alternative finance programs, including crowdfunding, special purpose acquisition companies (SPACs), private investments in public equity (PIPEs), and registered directs.

I have spent nearly 10 years after the passage of the JOBS Act working with the leadership of the crowdfunding movement, traveling extensively domestically and abroad, including dozens of trips to D.C., to provide our views on the proposed and final Regulation Crowdfunding and various JOBS Act rules and regulations.

I am legal advisor to the Association of Online Investment Platforms, the leading voice in D.C. for the industry. I am also a co-founder of two legal technology companies catering to the broader crowdfunding industries, one called LawCloud and the other called GUARDD.

My comments are my own and not on behalf of my firm, my clients, or the associations with which I am affiliated.

Given today's volatile market conditions where capital is scarce for entrepreneurs, not unlike the period right before an overwhelmingly-bipartisan congressionally-enacted JOBS Act, the timeliness of today's hearing is more important than it has been in the last decade.

According to the data published by Crowdfund Capital Advisors, from the inception of crowdfunding in 2015, to 2019, my last testimony here, there was \$193 million raised in the aggregate. From 2019 until today, \$1.4 billion has been raised. That is a sevenfold increase, which clearly demonstrates the commercial acceptance and viability of what Congress collectively put into motion in 2012 with the JOBS Act.

There have been over 4,300 funded transactions, 3,500 just since 2019. We have empowered a nationwide footprint of entrepreneurs to access capital to fund their American Dreams and create jobs, several of whom are with us. And it is exciting to meet them and see their vision come into reality, quite frankly.

We have created 225,000 jobs. Although the studies are limited, the data indicates that of these funded transactions, 55 percent of them have at least one woman or minority founder, have an 81 percent success rate, and represent nearly 48 percent of all capital raised.

We can all be very pleased with the results of crowdfunding, which would not have been implemented without the support of all constituents represented here. Regulators were decidedly uncomfortable with the idea of crowdfunding, and many of their stated concerns did not materialize.

Had we not proceeded and acted together, our economy wouldn't have benefited and, more importantly, these entrepreneurs would not have been funded and been able to hire employees. It is a wonderful example of Congress taking action that has had a very positive real world impact.

On a personal note, since my last testimony, my fellow panelist, Renee Jones, left her professorship at Boston College Law School to be appointed Director of the Division of Corporation Finance at the Securities and Exchange Commission; and Mike Piecek finished his time as head of the Department of Financial Regulation of the State of Vermont to be elected as the State's Treasurer.

As you might suspect, I am a little disappointed that my status remains unchanged, but I remain hopeful that my testimony here today may have a similar impact on my professional resume as it has for my esteemed colleagues.

I look forward to sharing my views on many of the proposals that will be discussed at today's hearing, and I thank Chairman McHenry for hosting this important hearing today. Thank you.

[The prepared statement of Mr. Ellenoff can be found on page 41 of the appendix.]

Chairwoman WAGNER. And we thank you.

Ms. Gladney, you are now recognized for 5 minutes to give your oral testimony.

**STATEMENT OF DEBORAH GLADNEY, CEO AND CO-FOUNDER,  
WORKTORCH**

Ms. GLADNEY. Chairwoman Wagner, Ranking Member Sherman, and members of the subcommittee, thank you for the opportunity to appear here today.

My name is Deborah Gladney, and I am the CEO and co-founder of WorkTorch. We are a career platform for service workers based in the heartland of Wichita, Kansas. I am honored to be here today with my sister and co-founder sitting right behind me, Angela Muhwezi-Hall, and to be present for such a critical agenda that impacts entrepreneurs like us from across the country.

When we started our company at the peak of the pandemic, we had no idea our company would take us to the places we have been, help the people we have helped, or allow us to see the things we have seen, things such as the extreme disparities in access to resources and capital amongst entrepreneurs.

Last year, startups with all-women founding teams like ours received just 1.9 percent of all venture dollars. And as Black founders, we received just a mere 1 percent. As if the odds aren't stacked up against us enough, 75 percent of all venture capital investments go to just three metro areas, and I can promise you that Wichita, Kansas, isn't one of them.

According to the data, my sister and I, as Black women founders in Kansas, should not be here in front of you today. What made the difference, you ask? We had our first example of hard work

from our parents. They came to this country from Uganda and worked hard to obtain their doctorate degrees, all while raising their five children, with no support or generational infrastructure built in this country.

They were our first example of what it means to be an entrepreneur, to build something out of nothing, to be scrappy and resilient, even if you are told no a hundred times a day, to take risks, even if it means leaving what feels comfortable, for the chance at building something big, even if it means me walking away from a comfortable salary while 8 months pregnant to build WorkTorch, or even if it means my sister leaving an esteemed university in beautiful Los Angeles to live in my basement with her husband as we built our company.

We did it because we knew building WorkTorch not only had the power to change our lives but the lives of service workers and their families. Every single day, our company helps people find fulfillment in life while being rewarded for what they do. But without our parents' example, I don't think my sister and I would have made it this far.

When we started WorkTorch, we had no connections or family or friends we could lean on for capital. We cold-pitched 379 investors, and we received 379 noes. We had to pull money from our own 401(k)s to build our product. But with our little money, we created a platform that garnered over 1,000 users in the first few weeks without receiving a dollar from anyone.

The scrappiness our parents taught us is what got us to the point of eventually becoming the first Black women in Kansas to raise over \$1 million in venture funding. But we also had to come to the table with twice as much to often receive twice as less.

It is also hard for us to be proud of the fact that in 2023, we are still seeing a lot of firsts for minority and rural entrepreneurs. Access to capital is literally stunting the ability of many businesses like ours to grow, and this is why today's proposed bills are so important.

Wouldn't it be great if more people who looked like me could invest in more people who look like me? The simple fact of the matter is that who gets funded depends a great deal on who is doing the investing. As a nation, we know the benefits of encouraging entrepreneurship across backgrounds. We create jobs, we spark innovation, and we allow America to maintain its position as the most-competitive nation on the planet.

So it is in our nation's best interest to foster more firsts like my sister and I and create more seconds and thirds and fourths and beyond to where we won't even have to count anymore. It is my hope you will be on the right side of entrepreneurial history today, and I look forward to your questions.

[The prepared statement of Ms. Gladney can be found on page 49 of the appendix.]

Chairwoman WAGNER. Thank you, Ms. Gladney. I am so glad that you and your sister are here with us today. Congratulations.

Ms. Howe, you are now recognized for 5 minutes to give your oral testimony.

**STATEMENT OF DARCY A. HOWE, FOUNDER AND MANAGER  
DIRECTOR, KCRISE FUND**

Ms. HOWE. I have heard this story a lot, and I am still verklempt.

Chairwoman Wagner, Ranking Member Sherman, and distinguished members of the Subcommittee on Capital Markets, I am Darcy Howe from America's heartland, Kansas City, Congressman Cleaver's territory—go Chiefs—and I have seen barriers to capital access firsthand.

As Deborah said, 75 percent of the venture capital to invest in technology startups comes from three States: California; New York; and Massachusetts. There are bold, innovative ideas to solve business and societal challenges in every county in this country, and they have gone unfunded, and that was a contributor to the slow economic growth of my region in Kansas City.

In 2015, Kansas City business leaders realized that after the 2008 downturn, we did not bounce back as well as peer cities like Indianapolis and Nashville. Many in our community set out to bring solutions to the region. And my volunteer assignment was to understand what was happening in entrepreneurship.

What I learned was that 70 percent of all net new jobs in the Kansas City area come from someone who is starting a business: 70 percent. But those starting high-growth technology businesses were leaving the area because capital was on the coast. Further, I learned that most rural entrepreneurs, people of color, and women were not getting funded at all.

So, what did we do to bring inclusive capital to Kansas City? With friends, we started an angel investing group to invest in women-led businesses called Women's Capital Connection. Then, I decided to retire from a successful 32-year career as a wealth manager and devote these past 6 years to raising capital and funding amazing innovators like Deborah and Angela in our region through the KCRise Fund.

Illustrating success when capital and innovators are connected, in 6 years, the 46 portfolio companies in our fund have created more than 1,000 jobs at an average wage of \$98,000. And, by the way, the average wage in Kansas City is \$45,000, which is our starting wages. If our 46 companies were one company, we would now be the 40th largest company in our region, and virtually none of these thousand jobs even existed 7 years ago.

In the past 3 years, 62 percent of our investments included at least one founder from at least one underrepresented demographic. Fifty-one percent of the employees—people think about founders, but think about the employees' generational wealth that they are building in skills—of our portfolio companies came from an underrepresented demographic. These inclusive statistics far exceed coastal venture-backed businesses.

You have now met one of our amazing founders, Deborah Gladney, and can see why investing in WorkTorch was not a hard decision for me and my partners, Ed Frindt and Liam Reilly. KCRise Fund invested \$400,000 and made introductions to venture capital firms in other parts of the country, which led to 4 more firms investing, for a total of \$1.1 million. And I will add parenthetically, Steve Case from here in D.C. was one of them.

As the eyes and ears of our region for VCs around the U.S., our support was validating to other venture firms in our network, which made her raise successful.

So, tell me again why we need these seven bills if all of this is working so great. I can speak to the DEAL Act, SEED, HALOS and ICAN.

ICAN is the bill which would unlock the most access to capital for small venture funds like KCRise. Our first fund was \$19 million and it took me 2 years to raise. Limited to 99 accredited investors, I had to find people willing and who had the resources to invest an average of \$200,000.

For Fund II, we wanted to increase capital in the region so we set out to raise \$40 million, and now our investors had to have \$400,000, on average. Not every small venture fund manager has a network like I have built over 30 years, and even I had trouble raising for startups, a type of investment that most people in the Midwest had never done before.

Please don't confuse us with the big-time private equity bunch with mountains of money. There are hundreds of small funds like ours springing up in smaller markets, and we would all benefit from raising the limit on our total number of investors.

It would accomplish three things—I realize I am getting close on time. First, it would allow more folks to participate. Funds could take smaller investors, really bring democratizing capital and be more inclusive. Second, being able to take more investors, we can more easily build a larger fund. And third, more people would get off the sidelines like me to do it. Funds are expensive. We have back office, we have rent, we have audits. Making a fund a little bit larger would make it possible to have a small team to help entrepreneurs.

More-inclusive capital is the lifeblood of new jobs in all counties over this country. And we are seeing already in our region in Kansas City that generational prosperity is broadening due to our focus and increased capital.

[The prepared statement of Ms. Howe can be found on page 51 of the appendix.]

Chairwoman WAGNER. Thank you, Ms. Howe, very, very much.

Ms. Thornton, you are now recognized for 5 minutes for your oral testimony.

**STATEMENT OF ALEXANDRA THORNTON, SENIOR DIRECTOR,  
CENTER FOR AMERICAN PROGRESS**

Ms. THORNTON. Chairwoman Wagner, Ranking Member Sherman, and esteemed members of the subcommittee, thank you for the opportunity to appear before you today to discuss capital access for entrepreneurs and small businesses.

My name is Alexandra Thornton. I am a senior director focusing on financial regulation and tax policy at the Center for American Progress, an independent nonpartisan policy institute dedicated to improving the lives of all Americans.

Today, more businesses have raised more money from borrowing, selling equity, and selling debt securities than ever before. In fact, banking regulators are worried about a collapse, securities regulators are worried about the proliferation of frauds, and investors

are worried that many private company valuations are unjustifiable and unsustainable.

In addition to seeking a loan from a bank, small businesses today can turn to the capital markets. After decades of deregulation by Congress and the SEC, a company can raise an unlimited amount of money from an unlimited number of sophisticated investors without making any meaningful disclosures about its financials, governance, operations, or risks.

Moreover, unlike banks and their employees, private equity and venture capital firms that raise capital and invest in businesses are generally not expected to follow regulator-mandated standardized documentation requirements and regulatory oversight of their capital allocation decision-making or the fees that they charge.

Venture capital and private equity funds are larger than at any time in history. Small businesses ought to have no problem obtaining capital in this environment. The problem is not that the rules prevent small businesses from obtaining capital. It is that the rules today allow companies with billion-dollar valuations, billions in revenues, and thousands of investors to continue raising private capital without providing basic information to investors, regulators, or the public, and private funds to raise billions of dollars from underlying investors without basic information about their procedures around capital allocation and portfolio management or the fees they charge.

SEC Chair Gensler said very recently that there may be as much as \$250 billion in fees in private funds each year, and much of that money isn't going to portfolio companies, including small businesses. There is also no regulatory requirement that these billion-dollar companies and funds provide investors with basic audits to ensure that financial information is accurate and reliable.

When Congress established the Federal securities laws in the wake of the Great Crash of 1929, it concluded that without basic information about a company, capital will be misallocated and wasted. So, it established the fundamental bargain that companies that want to raise capital from the public must first provide basic information to investors and the public, including the company's financials, governance, operations, and risks.

Today, these disclosures, along with robust audits, improve price discovery, make markets more fair, more orderly, and more efficient, and protect investors from abuses.

It goes without saying that even the most-sophisticated investors can't exercise their superior knowledge and expertise if they don't have reliable information about a company's financials, operations, and risks.

For decades after the securities laws were first adopted, offerings to even a single person or to a small number of employees were deemed to be public offerings in need of registration. But beginning in 1982, with the promulgation of Regulation D, Congress and the SEC began expanding the number of exemptions from the public disclosure framework, often with the stated intention of providing more access to capital for small businesses, just as many of the bills before the subcommittee today are saying.

But in reality, those exemptions, along with a few other provisions in the law, have enabled virtually any company of any size

to obtain capital from the public without complying with the public disclosure framework. A growing number of companies are choosing to remain private, and the majority of capital today is exempt from the public disclosure framework.

Today, more than 650 U.S. private companies are worth more than a billion dollars each in the private markets, and they too rely on these exemptions. They compete with similar publicly-traded companies and sell products and services to a broad swathe of the American public without making meaningful disclosures. They can pose huge risks to their investors, who include the teachers, firefighters, municipal workers, students, professors, and many others who have a significant amount of their hard-earned college and retirement savings invested in the private markets. Failure of any of these unicorns could have catastrophic consequences for these investors.

Expanding exemptions from public offerings will only make the wealthiest private investors richer, and it certainly won't help truly small businesses in underserved communities.

There are many steps that Congress and the SEC can take to rebalance the public and private markets and make more room for capital for small businesses. I look forward to discussing those with you. And thank you again for inviting me to testify today.

[The prepared statement of Ms. Thornton can be found on page 53 of the appendix.]

Chairwoman WAGNER. Thank you, Ms. Thornton, very much.

And thanks to all of our witnesses for your testimony today.

We will now move into the questioning portion of the hearing, and I will recognize myself for 5 minutes.

Mr. Ellenoff, as I am sure you are aware, Democrat SEC Commissioner Crenshaw gave a very concerning speech last week in which she cited growth in our private markets as a reason to increase disclosure and impose other regulatory obligations on private companies. In our view, her comments demonstrate how Democrats would rather force companies to go public than reduce barriers to capital formation for all, all companies.

Mr. Ellenoff, if the Democrat-led SEC moves forward with and eventually finalizes proposals that increase burdens on private companies, as it likely will in its forthcoming proposed rulemaking to revise Regulation D and Form D, can you explain how that would harm the millions of businesses that remain private?

And what I am really trying to get to is, would it make it harder for them to raise capital, create jobs, raise potential, or would these policies considered today, on the other hand, make it easier for small businesses to grow?

Mr. ELLENOFF. It is a troubling coordinated narrative that we are hearing. I think there is no doubt that increasing disclosure and pre-filing submission requirements on those issuers would be very problematic for a marketplace that has been around since 1982 and has operated efficiently, and successfully, by the numbers that we heard from Representative Sherman earlier, a \$4 trillion marketplace.

I don't know why we would even consider going about regulating it in a similar manner to what we did with our public company universe. These companies chose, tactically, to not go to the public

markets because of the overregulation within the public market sphere and particularly over the last year.

I think you would end up seeing a reduction in the capital-raising process. I think the securities offering supply chain—yes, I will take credit for that term—would become bogged down. I think it would be unwise, and I would steer clear of it.

And the thought process that somehow you can—as a securities lawyer, it would be a boon for me. So, when a securities lawyer is telling you not to do something, even though it would benefit me personally, I think you should take that under advisement.

I think to force large companies that choose to remain private, which is the same conversation we had in 2019, so the question is, how do you incent them to become public? And the thought process to burden private companies more is the incentive to get them to become public seems misguided to me and quite troubling.

Chairwoman WAGNER. Thank you very much.

Ms. Howe, as an angel investor, you have helped countless early-stage companies in my home State of Missouri and beyond raise the capital that they need to grow. In doing so, you have supported founders and their communities. You have also witnessed some of the barriers that exist which prevent startups from reaching their potential.

From your experience, could you provide examples showing how the policies considered today would benefit the early-stage companies in which you invest?

Ms. HOWE. First, maybe going back to Ms. Crenshaw's report, and maybe addressing Ms. Thornton, I hear a lot of, "unicorn," and, "billion dollars." These are companies that we are investing in them at \$5 million to \$10 million or \$15 million, and they will probably sell somewhere between \$50 million and \$400 million as a bolt-on to some other business.

The kind of businesses that we invest in tend to start smaller and they exit smaller as well. And so it is a different mindset than maybe some of the understandable concerns about regulating much-larger companies.

I would also say that we turn down investors. We had investors who were much more diverse, frankly, both in age and gender and ethnicity, because they couldn't afford to invest in a fund that had an average need of \$400,000 per investor. So by broadening it out, I think we would have much more inclusive capital.

And I would also say that one of the things that is troubling to me and I agree with the protections for—I was in the financial services business for 32 years. We need protections. But a fund format like we have, like all of these small funds that are being formed—by the way, and we have audits as well. But a fund format is a more diversifying, derisking way for people to invest and to participate in their neighbors, their kids, the people they want to invest in who are in their own local community.

Chairwoman WAGNER. Thank you very much, Ms. Howe.

I have a fantastic question for you, Ms. Gladney. I am going to submit it for the record since my time has expired.

I now recognize the ranking member of the subcommittee, Mr. Sherman, for 5 minutes.

Mr. SHERMAN. Some have said that sometimes the system doesn't fund somebody's business idea. I would say that is actually a good thing. Most ideas shouldn't be funded. I have a dozen ideas every day, most of them bad. And if you take a look at the bills submitted here in Congress, most of them shouldn't be passed.

The chairwoman says that there are millions of companies that are private that should stay private. I couldn't agree more. But there are a few dozen, just a few dozen that we should encourage to become public that are large enough to easily deal with the cost of being a public company.

If these companies become public, then we get more information about them, both in terms of trying to look at our society but also for investors. They can afford to do it. And then, the retail investor can get the liquidity of a publicly-traded company, the information, the analysis of a publicly-traded company.

We are here trying to decide whether to in some cases liberalize or in some cases tighten the rules for what it is to be a private placement or a non-public offering. We dealt with one of those this morning, changing the definition of, "accredited investor"—we had a whole hearing focused on that.

Doug, can you identify one other proposal that you would have to liberalize or to make tighter the rules here for private placements?

Mr. ELLENOFF. For private placements, I think there are several proposals before us in terms of increasing the caps. If you are asking about me to freewheel and come up with a new idea on rules to make private placements better—

Mr. SHERMAN. It doesn't have to be your original idea. Pick one idea you like, even if it is—most ideas are stolen from someone else.

Mr. ELLENOFF. I think we all can take a collective pat on the back for what we did in the JOBS Act in 2012. I think that is directionally what we ought to be doing.

Mr. SHERMAN. I now want to go to Ms. Thornton. You might have opposed the JOBS Act. I voted for it. I didn't think it was perfect, but I think it has done relatively well.

Can you identify one or two specific ways in which we should tighten it a bit without eliminating its basic concept?

Ms. THORNTON. Sure. Thank you, Congressman Sherman. I think one of the most important things would be to change the holder of record definition, because in the JOBS Act it was increased from 500 to 2,000. And when Section 12(g) was enacted in 1964, there wasn't a whole lot of difference between shareholders and holders of record.

But over time, because of technology and so forth, holder of record can now mean—one holder of record could be an intermediary that holds tens of thousands of shares from thousands of investors. And that is one holder—

Mr. SHERMAN. Now, it is one thing if you have an investment fund. Berkshire Hathaway might own a piece of a company, and we would count that, I would think, as one shareholder of record, because they are really making the decisions, even though I might own a share of Berkshire Hathaway stock.

But in a circumstance where, say, I have an account at Merrill Lynch, and so do 100 other people. They have all invested. We are all making our own individual decisions. And you are saying that if 100 Merrill Lynch customers are all in a stock, that it could be identified as one holder of record?

Ms. THORNTON. I believe that is right. And the thing about this threshold is that once you go above 2,000 holders of record, the company has to make significant public disclosures. And that is as it should be, because they are obviously a big company. This is the way that Facebook remained private for so long.

Mr. SHERMAN. And we might just set dollar amounts, say, we don't care if you only have 50 owners, if you are worth half-a-trillion dollars, you can afford it. We want the information. Your shareholders might benefit from it. And also, we are trying, in some cases, to push public companies in the right direction.

I know what is controversial is ESG. What is probably less controversial is an idea I proposed on the House Floor yesterday, and that is for companies to disclose and analyze how they would be affected if we had a breakdown of our relationship with China, because there are a lot of companies out there who are—what should I say?—pre-balloon in their thinking.

So, there is a benefit to companies going public when they are big enough to deal with the cost.

And I yield back.

Chairwoman WAGNER. The Chair now recognizes the gentleman from Arkansas, Mr. Hill, who is also the Chair of our Subcommittee on Digital Assets, Financial Technology and Inclusion, and the Vice Chair of the full Financial Services Committee.

Mr. Hill, you are recognized for 5 minutes.

Mr. HILL. Thank you, Madam Chairwoman.

And thank you again for continuing this theme of how we enhance capital formation for businesses of all sizes. I thought this was such an interesting group of legislative proposals and such an informed, excellent panel. Thank you all for being here.

Before I was in Congress, I spent a lot of time doing Reg D investments, and I thought many of these reflected some of the things that we have seen over the last decade, after the JOBS Act, of what we could tweak and fine-tune even better.

And on the subject of going public, look, it has just gotten so expensive to be a public company, and the liability is so high that, sure, the market cap has just gone up and up and up. When I first started my career, if somebody had a \$250-million market cap, they could easily be public and bear the cost, and we had more than double the public companies that we have now.

That is why you see so many enormous market caps, and I think that is why you see a big incentive for so many growth companies to stay private longer. I don't know if it is a chicken and egg thing. I take Ms. Thornton's point. I started my career in 1979, so I remember the 1982 amendments and I know where she is coming from, but I don't think that is a chicken and egg thing. I think that, really, it is the cost that has driven market caps up and the number of public offerings down, personally.

Entrepreneurs and small business folks are the backbone of all of our small towns, and I am so glad we have Missouri so well-rep-

resented here. I represent Little Rock, Arkansas, and I work with our venture ecosystem throughout central Arkansas.

And it is frustrating when you recognize that the top 20 metros in the country get 88 percent of the venture capital funding in the country, but due to the Kauffman Foundation in Missouri, and Steve Case's evangelism, this idea of making sure that we have a venture ecosystem open to all investors of all types has really seen a renaissance in the last decade.

The best ideas in this country are not reserved to the salons of Palo Alto or New York. Last year, Arkansas companies raised \$107 million in venture capital funding, 3 times higher than 2020. And while that is dwarfed by many States, it is indicative of the fact that our angel investor groups and our venture ecosystem is growing and growing successfully around the University of Arkansas at Fayetteville, and certainly in Little Rock, in and around The Venture Center, and accelerator programs that we have in Conway, Little Rock, and North Little Rock.

Unfortunately, entrepreneurs in many parts of the country face challenges to raising the capital they need. We just had a bill on the House Floor last week that we all supported which enhanced the SEC's studying, what are the barriers to rural capital-raising for people who are not even in a metro area? And I think your comments on that have been very, very helpful.

So, Ms. Howe, with your 2 decades of experience both in the brokerage business and now as an angel investor, how do these ideas today directly help a start-up dreamer in Kansas City or Little Rock?

Ms. HOWE. Our networks are only so large to be able to raise capital from our own personal network. And one of your—if you are speaking to the fund of funds bill as one example, I can give you an example.

Bringing Steve Case back up, 6 years ago, Steve Case and his whole Rise of the Rest came out to the Midwest and invited 20 of us who were brand-new fund managers to D.C. to learn from one another and support one another. And he asked us, how can we help you? And every one of us—by the way, nobody had ever raised more than \$30 million. That was our ceiling in our markets. And all of us said, "Steve, if you would just invest in our funds, you would give the Good Housekeeping seal of approval. And then, other people would understand and they would believe it and then we would get people who have never done this before, who were accredited investors, of course, off the sidelines."

So, this idea of the fund of funds would be really dreamy for all of us, because there will be investors that are in other parts of the country who would probably love to invest in WorkTorch, but they can't find them. And the way they could find them is through funds like us, who are boots on the ground finding—

Mr. HILL. Thank you very much.

Ms. HOWE. —and helping entrepreneurs.

Mr. HILL. I am glad to see a Morgan State Bear here. That is good. I co-Chair the Historically Black Colleges and Universities (HBCU) Caucus here in the House, so it is good to see Morgan State represented.

These ideas to expand crowdfunding—any thoughts on how you think that would benefit entrepreneurs in your world?

Mr. CONWELL. There are a lot of entrepreneurs who don't have networks, especially entrepreneurs who look like me. When I started my first company in 2010, I didn't know what an investor was. I didn't know where to go. I didn't know where to meet them. And when I did, I didn't know how to talk to them.

But that has no bearing on an entrepreneur's ability to execute. An entrepreneur can go to crowdfunding and say, hey, I have executed. I have done well. Who would like to take part in what I am building?

Mr. HILL. Great response. Thank you so much. And I thank all of you for being here today.

I yield back.

Chairwoman WAGNER. The Chair now recognizes the gentleman from California, Mr. Vargas, for 5 minutes.

Mr. VARGAS. Thank you very much.

Madam Chairwoman, what are we doing after dinner? We have had two hearings so far, one after breakfast, and one after lunch. I assume we will have one more meeting after dinner. It has been, again—

Chairwoman WAGNER. I will buy.

Mr. VARGAS. Okay. Great.

And I hate to challenge my good friend, Mr. Sherman, but Mr. Sherman used a term that he didn't define, and I think it would be very hard to define at the moment, and that is, "pre-balloon." We don't know exactly how long the balloons have been flying over our country, so we don't know exactly when the pre-balloon era started.

Mr. SHERMAN. If the gentleman would yield, I will point out we are now post-balloon.

Mr. VARGAS. We are post-balloon now. Okay. That makes more sense to me.

Again, this has been very exciting, actually, to listen to all of you, and I appreciate it very, very much. I do have some questions obviously.

Ms. Thornton, you said we should re-balance the public-private market, I believe. And how should we do that?

Ms. THORNTON. One way is the way that I mentioned to Congressman Sherman about modifying Section 12(g) to say that holder of record is actual shareholders, beneficial owners of securities.

Another, of course, would be what he alluded to, which is to say that large companies that have a certain value are subject to the public disclosure framework, or you could say that companies that have a certain number of employees would need to comply with the public disclosure framework.

And aside from that, I think that it is really important for policy-makers, for Congress, and for the SEC to look at the existing exemptions and consider whether they really are doing what we think they are doing and what we want them to do.

When you look at what is going on right now, just because an exemption is expanded to allow retail investors who are less wealthy to participate and to invest in these funds, doesn't guar-

antee that there will be more investment in businesses run by women and minorities.

Doubling down on a system that—we have had, I think I counted 14 expansions of the different exemptions since 1982, including the 1982 Reg. D. And doubling down on a system that is already shown not to promote women and minorities is unlikely to help. So, I would encourage you to think about that and to look at the different exemptions and consider how they might be scaled back.

Mr. VARGAS. Mr. Ellenoff, I think it would be appropriate to give you an opportunity to respond to that. What would you think about those?

Mr. ELLENOFF. I appreciate the opportunity. I have in front of me the Annual Report from the SEC's Office of the Advocate for Small Business Capital Formation, and they have two bubbles in crowdfunding that I think may be instructive and responsive to that comment.

Forty-one percent of crowdfunded issuers that raised \$1 million or more had minority founders. Another thought bubble: 46 percent of crowdfunded issuers that raised \$1 million or more had women founders.

And I would encourage everybody on the committee to go and review this annual report, and I think you will see outstanding statistics that support not only that underrepresented people raise money much more effectively, pursuant to these JOBS Act exemptions, including Reg A+, 506(c), but if you look at the geographic dispersion in their charts, along with what is on Crowdfund Capital Advisors site, you will see that almost every State in the Union is represented, as opposed to what happens with 506(b) venture deals.

Mr. VARGAS. Thank you.

I do want to challenge one premise that I think is underneath all of this—or not challenge it, but ask about it, and that is the issue of returns, that the private markets have better returns, in general, than the public markets. Back in 2019, we had Professor Elisabeth de Fontenay testifying that that is not the case, to my understanding.

Could you comment on that, Ms. Thornton?

Ms. THORNTON. Sure, I would be happy to. When you look at the private markets, private market participants don't have to disclose information. So, that should be a red flag right there. Even the financials that they do disclose are not necessarily audited by independent auditors. And the information often isn't timely. There is information given to some investors that is not given to others.

What does this create? This creates an environment where valuations can be inflated. And there is copious evidence that valuations are inflated in the private markets.

What happens is these companies, when they go public, that becomes—they stay in the private markets for a long time because they can raise a lot of capital now that there are all these exemptions. But when it comes time to cash out, when the original investors want to cash out, they do an IPO, and the retail investors invest, and they are the ones who lose out because the company was overvalued.

There is evidence—I think Goldman Sachs did a study which showed that something like 28 percent of the companies that went through IPOs like this declined in value tremendously.

Mr. VARGAS. My time is up. Thank you very much.

Thank you, Madam Chairwoman.

Chairwoman WAGNER. The Chair now recognizes the gentleman from West Virginia, Mr. Mooney, for 5 minutes.

Mr. MOONEY. Thank you, Madam Chairwoman.

Nearly 20 percent of the U.S. population lives in rural areas, and yet businesses in rural areas raised under 2 percent of the total capital over the last 3 years. In my home State of West Virginia, no city even has a population greater than 50,000 people, in the entire State.

So, Ms. Howe, can you elaborate on some of the capital-raising trends for small businesses in rural areas versus those in big cities? And as a followup to that, why is there such a large discrepancy in the trends?

Ms. HOWE. I'm sorry. Can you repeat the follow-up question?

Mr. MOONEY. The second part of that is, why is there such a large discrepancy in the trends?

Ms. HOWE. First, my brother played basketball for West Virginia.

Mr. MOONEY. Okay.

Ms. HOWE. I am not sure I completely understand the question about the trends, but the trends clearly, in our market, when—and what I see in my other fellow small-fund folks who are building small funds in other States, because we are co-investment models, so we have to have another venture investor in our realm in order to invest.

And what I have seen is it has broadened out who—people like me—I am 66-years-old, female—are starting funds. They are not all young, White males. So, we all have different experiences, and I think these smaller funds are being started by people who then are broader in thinking in how they look at the kinds of deal flow they might look at.

There is one proposal I have seen regarding angels and demo days, and I would like to address that in some of those smaller areas.

The reason why Silicon Valley became Silicon Valley is because of the network effect. They knew each other. They were in a small community. It was like a small town where the investors and the entrepreneurs got together and helped one another, funded one another. We need that in our smaller towns. And demo days are a very important way for angel investors, curiosity seekers, people who want to help these entrepreneurs, again, who are their neighbors, or their kids, or their friends' kids, or whomever, to help them.

So, I think the basket of proposals that I see here each help in a little different way. I don't think you could prioritize them, because I think a place like West Virginia, where you have demo days—a demo day in a small town where you have two or three entrepreneurs who are starting something who just want to get a forum and get their idea out there and see if there is somebody who can help them is critical to them getting funded and finding resources and advisors and people who will help them.

Does that answer your question?

Mr. MOONEY. Yes. Thank you very much. I was just trying to get an idea of what you think the trends are and what is happening.

My next question is for Ms. Gladney. What are some of the unique challenges rural small businesses face and what can be done to address them?

Ms. GLADNEY. Thank you for the question, Congressman.

The biggest thing that I have experienced and I have witnessed is that this is a relationship-based industry. So, if you are living in an area that does not have an established ecosystem or established network, then you have no network.

And unfortunately, the way that the system is currently set up right now, it doesn't bring people in; it keeps people out. And that is what is happening to rural entrepreneurs. If you are not connected to the ecosystem, if you don't have that within your community, then it is extremely difficult for you to infiltrate the system.

Mr. MOONEY. Thank you.

I assure you, rural poverty is real. It is not just in the big cities. Internet connectivity is an issue, especially the high-speed internet. The bases of population where you can crowdfund may be harder to find.

Last week, the House—and thank you for the bipartisan support—passed my bill, the Expanding Access to Capital for Rural Job Creators Act. It simply requires the Securities and Exchange Commission's Small Business Advocate Office to identify and report the challenges that rural small businesses face when trying to access our capital markets.

That is only one step. We must do more. So, I look forward to working with this committee to make sure rural small businesses aren't left behind as we face these challenges in West Virginia.

Thank you, Madam Chairwoman. And I yield back.

Ms. HOWE. May I add to that about the State Small Business Credit Initiative (SSBCI)? Thank you so much for SSBCI, because SSBCI coming down to the States—the State of Kansas, as an example, is using that. There is a lot of rural Kansas, right? They have 105 counties of rural everything, and they are using the SSBCI money to do all of the things to find and to support entrepreneurs in each county. So, thank you all very much for that money.

Chairwoman WAGNER. The gentleman has yielded back.

I now recognize the gentleman from Illinois, Mr. Casten, for 5 minutes.

Mr. CASTEN. Thank you, Madam Chairwoman. And thanks to all of our witnesses.

Ms. Howe, I have been sitting here reading your resume and thinking that in another life you and I might have run across each other. Before coming to Congress, I raised a lot of capital for privately-held companies.

When you were—I just want to understand a little bit about your background—at Merrill Lynch's private banking practice, was that primarily for—I assume that is like wealthy families and family offices who were your clients, is that right?

Ms. HOWE. Yes. My investors were families of wealth.

Mr. CASTEN. Okay. And was there a minimum size that you were targeting or a typical size? Just help us understand who your clients were, typically?

Ms. HOWE. Back then, my minimum size was \$10 million and up.

Mr. CASTEN. Okay. And were they investing primarily equity, or were you advising them across the whole capital structure, debt, mezzanine instruments, and everything else?

Ms. HOWE. The entire capital structure, including their philanthropy and multi-generationally.

Mr. CASTEN. Okay. And if they were investing in debt or mezzanine, were you actually negotiating debt deals, or was this where you would be negotiating covenants, or were you primarily backing into other, previously-syndicated deals?

Ms. HOWE. No. Merrill Lynch was pretty much a distribution of other people's investment ideas, so—

Mr. CASTEN. Okay. And did you make many direct investments outside of the public? Were you doing real estate? Would you ever advise them to make a direct investment in a new business like we are talking about here today?

Ms. HOWE. I made none on behalf of our clients, but I made personal angel investments.

Mr. CASTEN. Okay. I am thinking of this from the perspective of a family that has minimum \$10-million wealth. I am assuming they have some direct investments, whether through funds of funds, or they have a buddy they went to college with who is—the things you do as a private wealth manager.

Would you help with the diligence on those investments for them?

Ms. HOWE. Did I help with diligence?

Mr. CASTEN. Yes.

Ms. HOWE. Absolutely.

Mr. CASTEN. If you have a wealthy family saying, I need to do this, but I don't understand the financials and should I trust this auditor, those sorts of things that one gets into where they need a neutral party?

Ms. HOWE. Happily, it gave me 32 years of education to read financial statements because I am now on 11 boards of our portfolio companies, so yes.

Mr. CASTEN. I sometimes say that the best preparation I ever made for running for Congress was running a private equity-backed company because I learned to live with the fact that I was going to be surrounded by really smart 20-somethings telling me how to do my job. That is the nature of this line of work.

I ask all of those questions because I don't know how somebody who has \$10 million in personal wealth makes an informed judgment about how to invest in a privately-held company without having someone of your talents. It is just too complicated. Right? And, yet, now we are having this conversation saying, should we make it easier for people who can't afford to hire someone like you to run through those investments?

My question for Ms. Thornton is, as we talk about expanding access in private markets to people who can't afford to hire Ms. Howe, who are not worth \$10 million, who don't pass anybody's existing definition of a sophisticated investor, is it not our obligation

as Congress to provide them with the protections that they would otherwise get from someone like Ms. Howe?

Ms. THORNTON. Absolutely. In fact, I would submit that probably they shouldn't be going into the private markets. But if one is going to expand exemptions, it is really critical that that information be provided. And the bigger the exemption, the more information should be provided.

There is a reason why we have the public markets and why we have the disclosures. In the private markets—I'm sorry, did I say private? I meant to say the reason why we have public markets is for disclosure.

But what happens in the private markets is that there is no information. Values are inflated. The original people, Ms. Howe's clients, who originally came in and put money into that investment, whatever it is, can actually cash out, because we are also seeing an expansion of secondary markets in the private markets. They can cash out, and all those new retail investors who came in, who really couldn't afford to lose their money and, have bills to pay and can't afford a catastrophic loss, they are the ones who lose out. They don't get the benefit of the high valuation.

Mr. CASTEN. In the 25 seconds I have left, there are a number of bills that have been noticed and you have reviewed for this hearing. All would seem to make it easier for companies to access money from smaller investors.

Are there any of those bills, in your judgment, that provide greater protection along the lines that Ms. Howe used to provide?

Ms. THORNTON. I skimmed through them. I didn't have a lot of time between when I saw them and this hearing to go into detail.

I guess I would just say that, basically, the committee should look very carefully at what they are going to accomplish, actually, for small businesses.

Mr. CASTEN. Thank you. I yield back.

Chairwoman WAGNER. The Chair recognizes the gentleman from Oklahoma, Mr. Lucas, for 5 minutes.

Mr. LUCAS. Thank you, Madam Chairwoman, for holding this hearing, and thank you to the witnesses for testifying.

Businesses use both private and public markets to raise capital, and the committee is dedicated to ensuring both avenues are healthy for both companies and investors.

Public markets have enormous benefits to a wide range of investors and I will continue to support policies that strengthen public markets and encourage businesses to utilize public offerings. I also recognize that healthy private markets support our robust public markets and benefits both companies' investors.

That said, Mr. Ellenoff, could you discuss the advantages to companies' investors of having access to both public and private markets?

Mr. ELLENOFF. The democratization of access to deal flow, which is what the JOBS Act really did, established a mechanism by which investors from around the country could invest in deals in other parts of the country that they would never otherwise had the social networks to know that those deals were looking for money. And they post those deals on websites called funding portals that are staffed by investment professionals who do extensive due dili-

gence on the deals and respond to some of the concerns that were raised previously. And those deals are vetted so the investors can have access and invest in those deals.

Having access to early valuations, like is being suggested, is a problem in that if you don't get in on the earlier deals while they are private, you won't benefit from the increased valuations over time.

I think retail investors having access to both the public markets, which they do through their Merrill Lynch or E-Trade account, where they don't have other people doing diligence for them necessarily, is equally important to learning how to invest.

What is great about the crowdfunding provisions generally is there are caps in Reg CF that limit the amount of exposure that retail investors have. And as far as I know, after a decade, neither regulators nor commercial participants have been upset by the results over the last decade, which is a reason why we continue to liberalize.

Mr. LUCAS. Continuing along that line, Mr. Ellenoff, we are 10 years from the passage of the JOBS Act. Could you give us your perspective on what we are seeing in the economy that should encourage Congress to revisit provisions of the JOBS Act?

Mr. ELLENOFF. I will give you a statistic. I spoke to Sherwood Neiss, who is the godfather of crowdfunding, if you remember him traipsing through these halls in 2012. When we increased Reg CF from \$1 million to \$5 million, which we had wanted from the beginning, \$5 million, 435 companies in the last few years have now raised more than the \$1-million cap, which increases jobs, funding for entrepreneurs, helps individual States across the country and, again, minorities and women. Forty-five of those companies raised the \$5 million max.

So, why would we not increase it further in order to get more companies to raise more money to carry out the empowerment of the American Dream for entrepreneurs?

Mr. LUCAS. Thank you. Very insightful comments.

I yield back, Madam Chairwoman.

Chairwoman WAGNER. The gentleman yields back.

The Chair now recognizes the ranking member of the full Financial Services Committee, the gentlewoman from California, Ms. Waters, for 5 minutes.

Ms. WATERS. Thank you very much.

I would like to address Ms. Thornton.

Ms. Thornton, when most Americans think about our capital markets, they think of the New York Stock Exchange and stocks sold by large companies like Apple, Ford, or GE. However, many would be surprised to learn that the private markets now dwarf the public markets. And as I understand it, historically, the private markets were where small businesses raised capital. But today, even the largest companies now raise much of their capital there.

Can you provide a little more context as to how these changes have affected small businesses trying to raise capital and the impact on public markets? What do you think Congress should do or should encourage the SEC to do to support small businesses through capital markets?

Ms. THORNTON. Thank you, Ranking Member Waters. I appreciate the question.

I think that, historically, for about 5 decades after the securities laws were enacted, after the stock market crash of 1929, we had a situation where the courts interpreted, “public,” very broadly. So, sometimes in situations where there was one shareholder, a few of those companies were required to make public disclosures.

Then, with all of these proliferations of exemptions, the private markets grew. And as you said today, the private markets raise more annually than the public markets do. And the problem with that is there is no incentive for a company to go public, and that has serious ramifications for not just the people who invest in a company that is private, a company that doesn’t disclose financials that are independently audited, and so forth, but it also has ramifications when that company gets large and it sells products to American consumers. And if it runs into financial difficulties because it hasn’t been overseen by regulators, that can actually cause systemic problems in the capital markets.

That is another big part of the SEC’s mission. So in addition to ensuring that investors and companies have adequate information when they invest in those companies, the SEC also needs to be aware of the potential for systemic problems.

And we need to consider whether the situation we have gotten ourselves into needs to be rolled back a little bit. I think it makes a lot of sense to look at these exemptions and consider how they can be trimmed back, whether we really need or want big companies in the private markets, and whether we shouldn’t have a lot more disclosure for much of what goes on in the private markets.

Ms. WATERS. Let me continue.

Today, large private equity firms and multibillion-dollar tech companies have taken advantage of exemptions originally meant for small businesses. For example, between 2009 and 2017, pooled investment funds, most of which are private equity funds, have raised \$8.9 trillion of new capital through Regulation D offerings compared to \$1.42 trillion raised by non-funds.

What are your views on the uses and misuses of the exemptions originally meant for small businesses? Should multibillion-dollar private firms and private equity firms be able to use them?

Ms. THORNTON. Absolutely not. It is basically an abuse of the system, if you will, when these really large—when these unicorns, who have so much in assets and so much ability to raise capital, are using something like Reg D to raise funds. And I think Commissioner Crenshaw just a week ago mentioned this as well, how much of Reg D is actually unicorns seeking additional capital. It just creates risks for, as I said, the markets and also for the many people who invest.

Ms. WATERS. Thank you.

I am going to go to Chairwoman Wagner before I continue with these questions.

I would like to ask unanimous consent to submit a report for the hearing record that was released by the North American Securities Administrators Association entitled, “Report and Recommendations for Reinvigorating Our Capital Markets.”

Chairwoman WAGNER. Without objection, it is so ordered.

Ms. WATERS. I have a few minutes left here, and I just have a statement I would like to make.

Constantly, all that we hear from small businesses is, "I just don't have access to capital. If only there was a fair way to get access to capital, I know I could do well. I could expand. I could provide more goods, more services. I could do all of these things." And so, as we confront this issue, we have to find out what we can do.

Quickly, during the pandemic, with PPP, in that small period of time where we raised that money to get to small businesses, I want to tell you how helpful it was, how thankful they were, and how they were able to keep their employees, on and on and on.

With that, I yield back, because I could talk about that all day. Thank you.

Chairwoman WAGNER. The gentlelady yields back.

I now recognize the gentleman from Pennsylvania, Mr. Meuser, for 5 minutes.

Mr. MEUSER. Thank you very much, Madam Chairwoman.

Madam Chairwoman, first, I would like to request unanimous consent to enter into the record several letters: a letter from the U.S. Chamber of Commerce; and a letter from the Center for American Entrepreneurship.

Chairwoman WAGNER. Without objection, it is so ordered.

Mr. MEUSER. Thank you.

And thank you very much to our witnesses. It is quite informative. I appreciate it.

But I also appreciate our Chair of this Subcommittee, as well as our Chair of our Full Committee, Mr. McHenry, for this focus on and prioritizing of capital formation, especially for small businesses, and really working to build off of the JOBS Act.

I spent most of my life in small business, growing small businesses into a large business, and working with customers that were all small businesses, or virtually all of them. And I also sit on the House Small Business Committee, so these topics are extremely important to me.

Access to capital, cash flow is the lifeblood of a business, as we all know. Yet, all data continues to show, even this morning in a hearing, that only 13 percent of households of those who want to invest have the ability to be an accredited investor, and as well, only 19 percent of small businesses would state that they have adequate access to capital. So, we clearly have work to do.

And as well, last year, there was an enormous decline in IPOs, as you know. The numbers I have show 74 IPOs. Now, granted, the year before was quite high, but that is 3 times less than the typical average over the last 10 years.

So, what is going on? We need to remove these barriers or we can begin to start thinking about how many new-growth businesses, technology businesses, what have you, will not be created here and could be created elsewhere.

Ms. Howe, I would just like to ask you first, the Developing and Empowering our Aspiring Leaders (DEAL) Act of 2023, that was introduced last year, decentralizing investments, is this something that you think is very important?

Ms. HOWE. I'm sorry, that is the fund of funds act, right?

Mr. MEUSER. It is.

Ms. HOWE. I am getting all of these confused.

Mr. MEUSER. Yes.

Ms. HOWE. I think I addressed that a little bit earlier. The funds of—we are the most entrepreneurial country on the planet. How do we figure out how to continue to keep in our genius zone? And that is by broadening the access.

Broadening access in our world, in Kansas City and Kansas and Missouri, is to have other people know what kind of great entrepreneurs we have here. And having fund of funds have the ability to find—they won't invest directly into WorkTorch, but they would invest in our fund. And our little fund could use the extra capital. We have turned away hundreds of other investors.

Congressman Sherman is correct that there are a lot of deals that shouldn't get funded. But there are a lot that should, that don't get funded because we don't have the capital and we don't—we build syndicates of folks from outside our region. And the best way for us to build syndicates is what we do now, we just go out and we find other VC firms that might be interested, and we go out and sell the deal to other folks.

But in this case, for fund of funds, it would be so much easier for people to develop a fund because you get the Good House-keeping Seal of Approval of a Steve Case, or whomever else, that would say, yes, this is a venture firm that has a good track record, they know what they are doing.

Mr. MEUSER. Okay. Thank you. So, you are positive about that.

And the Improving Capital Allocation for Newcomers (ICAN) Act of 2023, expanding the eligibility for capital contributors?

Ms. HOWE. We are on our third fund. We have raised \$27 million of the \$40 million that we would like to raise, and we are already up to 70 investors. And we have a list of folks who would love to get in for \$50,000, but I don't know that we can take them, because we don't have room for them under the 99. So, if we had more room for investors, we could take much smaller investors.

And in a fund format, by the way, that is de-risking the riskier part of the capital stack. I believe strongly in smaller investors should be in funds.

Mr. MEUSER. There is no question, VCs—there is a saying: It is easy to count the seeds in an apple but not so easy to count the apples in a seed. So, I definitely commend the work that you are all doing. And we are very interested in hearing more from—I am just about out of time—all of you on what else this committee needs to do. I appreciate your time.

And I yield back, Madam Chairwoman.

Chairwoman WAGNER. The gentleman yields back.

The Chair now recognizes the gentleman from North Carolina, Mr. Nickel, for 5 minutes.

Mr. NICKEL. Thank you, Madam Chairwoman.

And thank you so much to the witnesses for being with us here today.

Small businesses are the backbone of our economy and of my district. In Congress, I am doing everything I can to ensure that they have adequate access to capital. Additionally, retail investors need the protections of our securities laws to ensure they have access to vital financial information. If a company is underperforming, these

non-professional investors would likely have a hard time accessing this information.

Ms. Thornton, how would removing disclosure requirements harm retail investors that our small businesses, especially our minority-owned small businesses, rely on for capital?

Ms. THORNTON. I think it is important to remember that if you are a small business, you are actually going to prefer having just a handful of really sophisticated, really experienced investors that you can go to when you need more capital. Having a lot more investors, retail investors, people who don't really know as much and really can't afford to lose their funds, can actually be harder for the small business if they have to respond directly to them, and also, if those retail investors need to pull out of their investment; typically, in the private markets, investments are locked up for some time. So, it is very difficult for retail investors in that case, and it is bad for the small business.

I think that the disclosures that we are talking about, making more disclosures is actually good good for the both the small business and the retail investors.

Mr. Ellenoff referred to democratization and how much due diligence is being done and all of that in his firm or the firms he works with. But, in reality, that is not required at all. It is not mandated. It is not overseen by the SEC. The SEC doesn't have that information.

But, also, if companies are doing this due diligence anyway, if funds are, if companies are providing the information to the funds that hold them or whatever, there shouldn't really be any problem with adhering to the public disclosure framework. They should be able to disclose more information.

Mr. NICKEL. Thanks.

Ms. Thornton, as you said in your testimony, if a company can raise all the capital it needs in the private markets without making disclosures, developing robust operational safeguards, subjecting itself to audits, or subjecting itself to SEC oversight and potential class-action plaintiffs, why would it go public?

Does the current exemption framework incentivize companies to stay private, therefore depriving investors of information that is important and meant to protect them?

Ms. THORNTON. Absolutely. It definitely, definitely encourages companies to stay private, to grow in the private markets and, really, never to go public unless, for example, the founders or original investors want to cash out.

And so, basically, we have a perverse, distorted system where capital now is being invested with no information, which is basically the situation we had before the stock market crash of 1929.

Mr. NICKEL. Thank you so much. And I yield back.

Chairwoman WAGNER. The gentleman yields back.

The Chair now recognizes the gentleman from Iowa, Mr. Nunn, for 5 minutes.

Mr. NUNN. Thank you, Madam Chairwoman. And I am privileged to have another Midwesterner sitting up here. Your appreciation for capital outside the venture capital bubbles of certain communities is much appreciated, and I think is something that we would like to talk about today.

As we sit here today, roughly 11 years after a divided Congress passed the Jumpstart Our Business Startups (JOBS) Act of 2012, we are still faced with similar challenges to help all entrepreneurs, many of you here in this room, as well as our Main Street shops, our small farmers, and the small businesses that grow off of them.

And, unfortunately, my perspective time and time again, is that D.C. has added costly bureaucratic red tape that interferes with my constituents' abilities to come here and serve well in this.

The House is determined to reduce regulatory burdens for small businesses and entrepreneurs at home. In my great State of Iowa, a record number of more than 33,000 new businesses were started in the last year alone, post-COVID. It is our responsibility to provide adequate funding opportunities for those who take this amazing leap of faith, as you have on this panel today.

Mr. Conwell, I would like to begin with you. When the JOBS Act was passed, one of the things that critics were most afraid of was that the law would dramatically weaken investor protections and increase fraud in the securities market. But 11 years on in the JOBS Act, those predictions have not come to pass. Congress has continued to work on bipartisan issues to build upon the JOBS Act.

In your view, how would a small business and entrepreneurs today in a State like mine, in Iowa, benefit from some of the new bills we are considering today?

Mr. CONWELL. One, you are now allowing for angel investors to be more active. And when you are talking about rural parts of the country, are you talking about States outside of the major tech hubs?

Mr. NUNN. Right.

Mr. CONWELL. They are all funded and backed and supported by those local individuals. It is so important for the angel investors to have the ability to do more.

Then, when we talk about the ICAN Act, it allows for more newcomer investors to have more opportunities to raise capital.

I wouldn't be able to raise capital if it wasn't for the JOBS Act and the 506(c) designation. And because of that, I now have investors in my fund from all over the country, and I am investing in companies from all over the country. Every investor is not going to do that, but it gives us the opportunity to have more investors with more ideas and more different ways to go about investing.

Mr. NUNN. I love that innovative spirit. Well done, and compliments on everything you have done there.

Ms. Gladney, I would like to speak with you on this as well. According to the SEC's Office of the Advocate for Small Business Capital Formation, small businesses have accounted for 66 percent of the employment growth over the past 25 years. However, 89 percent of entrepreneurs claim that access to capital is limiting their small business. In fact, 78 percent claim it is limiting their day-to-day operations, which is very scary for a small entrepreneur.

Could you please talk about your experience during your early stages with WorkTorch? And specifically, in Kansas, what was one of the most difficult parts for you to be able to start WorkTorch?

Ms. GLADNEY. Congressman, thanks for your question. And I was born in Ames, Iowa, so fun fact.

Mr. NUNN. There you go. Cyclone territory.

Ms. GLADNEY. Yes. And I appreciate that question, because I think so much—we talk about startups and small businesses once they are past that zero-to-one phase. That zero-to-one stage is so difficult.

So when my co-founder and sister, Angela, and I decided to start WorkTorch, we had so many barriers when it came just to even knowing or understanding. It was very clear that we were outsiders. We didn't even know there was an ecosystem that existed. So, of course, we didn't know the players. We didn't understand the language. We didn't understand any of that.

Even trying to get from zero to one was so challenging, which is why we had to do something so risky as taking our money out of our 401(k)s, because we were seen as outsiders.

The more that we can support entrepreneurs in those earlier stages, I think a lot of—unfortunately, a lot of businesses, they die in that zero-to-one ideation stage.

Mr. NUNN. I would agree with you on that.

Let me be quick on this, because I think this is an important thing for entrepreneurs like you across the country. As you know, Reg A or the Mini-IPO offering process is less-intensive and less-costly than the traditional initial public offering.

Do you think, based on your experience, it is time for Congress to revise Section A? Specifically, House Republicans are advocating that we raise the amount to \$150 million from the current \$50 million and include an inflation adjuster.

Would this have helped you?

Ms. GLADNEY. Absolutely. Just increasing the access, of course, absolutely, it would help.

I see that the time is running out, so I just want to keep it brief.

Mr. NUNN. Thank you for your service.

I yield back.

Ms. GLADNEY. Thank you.

Chairwoman WAGNER. The gentleman yields back.

I now recognize the gentleman from the Kansas City, Missouri, area, the soon-to-be Super Bowl champs, the Kansas City Chiefs, my fellow delegation member, Mr. Cleaver, for 5 minutes.

Mr. CLEAVER. Thank you for that opening objective analysis of the coming game.

I was going to ask Ms. Howe, before you said anything about the game, it doesn't mean we are bragging about anything. If you win, you are not bragging. And we are hoping that the rest of the committee members will come in and celebrate, at the next hearing, the Kansas City Chiefs as world champions.

I am glad we have some folks who have taken advantage of this. I have been on the Financial Services Committee for 18 years, but this is my first time on the Capital Markets Subcommittee. So in trying to get up to speed on it, I thought people are going to run away. A shareholder of record does not denote the current owner of stock. Instead, it suggests who owned it 2 days prior.

Now, if you tell somebody who is wanting to participate and go into business, won't they start getting a headache? Am I interpreting that correctly? Is that correct?

Mr. ELLENOFF. May I?

I think there is a misunderstanding here. Shareholder of record for public companies, it is true that often on a central ledger system called CD, multiple shareholders are centralized as one shareholder for purposes of calculating for proxy rules under the public company laws. For private companies, that is not really accurate. It is one-to-one.

I think if you ask any of the entrepreneurs or venture people here, you will find that the shareholders that are listed are their record holders. And while I can't say that is true in all cases, I can say it is in the predominance of cases.

The concern that I have when I hear questions like that is if the route the SEC intends to use to force private companies to go public is by playing games with 12(g), I think that is problematic.

Mr. CLEAVER. I appreciate that. Thank you.

Ms. Howe, and Ms. Gladney, can you speak to the challenges in fundraising for start-up companies, particularly those who are pre-revenue, thereby making bank capital largely inaccessible?

Ms. GLADNEY. Thanks for the question, Congressman. Definitely, the pre-revenue stage was the most challenging stage for us. And, again, not being an insider, you go to the websites of a lot of these investment firms that will say, hey, we invest at day zero. So we think, hey, we are at day zero, and we try pitching. And come to find out, more than likely they definitely—they don't, or it is not for people who look like me or people who don't have that existing connection.

So, it is extremely challenging, which is why it tends to put a lot of founders like Angela and I in a corner, where it is either we let this idea die or we pull out money that we probably shouldn't pull out to make it work.

Once we get the revenue in, at least we can start saying we have traction, and it mitigates some of the risk, and you will start to see more people come. But it is still even challenging at that point for founders like myself.

I will let Darcy kind of chime in before time runs out.

Ms. HOWE. Pre-revenue companies are the purview of angels. Angels are more predominant in markets where they have already made money and they are, "on house money." So, they can afford to take the risk of giving \$20,000 or \$30,000 to Angela and Deborah.

I don't think that is the right place for early, early investors, frankly. That is the place for people who are more sophisticated and who can help these young, young, young companies, if that answers the question.

Mr. CLEAVER. It does. Thank you.

Madam Chairwoman, I yield back.

Chairwoman WAGNER. The gentleman yields back.

The Chair now recognizes the Vice Chair of the subcommittee, the gentleman from New York, Mr. Garbarino, for 5 minutes.

Mr. GARBARINO. Thank you, Madam Chairwoman, and thank you very much for hosting this important hearing today. And thank you to our witnesses.

Madam Chairwoman, before I ask questions, I request unanimous consent to enter into the record several letters: a letter from

the Small Business Investor Alliance; and a letter from the National Venture Capital Association.

Chairwoman WAGNER. Without objection, it is so ordered.

Mr. GARBARINO. Thank you very much.

Mr. Ellenoff, I am going to start discussing Regulation A with you. Title IV of the JOBS Act directed the Securities and Exchange Commission to adopt rules examining securities offering up to \$50 million within a 12-month period from Securities Act registration requirements.

Upon implementation, the SEC created two different tiers: Regulation A, Tier 1, caps at \$20 million; and Tier 2 allows for the sale of \$50 million, which was later raised to \$75 million.

The benefit of having Regulation A is that it provides an opportunity for small and medium-sized private companies to access capital on a scale more appropriate for their needs with limited disclosure requirements.

Despite these benefits, you mentioned in your written testimony that Regulation A still needs to find its footing.

Can you explain why Regulation A has been underutilized? And how would amendments to Regulation A help small businesses raise capital? And would more companies benefit if Regulation A raised its offering cap?

Mr. ELLENOFF. First off, we have to recognize the great State of New York together, okay. If everybody else can do it, we should be doing it just because we are a big urban center.

Reg A+ is a more-involved disclosure document, not unlike a traditional IPO on an S-1. It is on what is called a Form 1-A, and it has extensive legal work, and accounting work involved. It takes months to prepare or weeks, in many cases, if it is an earlier stage company.

The good news—and I spoke to one of the founders of the big platforms this morning—is in the last few years, \$5 billion has been raised in Reg A+. So, it is an exemption that is getting traction. It is just not as much as I think regulators would like it to be.

And many of the major investment banks, the Mini-IPO, don't tend to follow in that direction. I think increasing it to \$150 million, which is the proposal from \$75 million, would be advantageous in that it may attract a higher quality number of Silicon Valley-based companies that may choose to use it.

The cost of doing a Reg A+ deal and the time and the sophistication kind of necessitate larger deal sizes in order to pay for the diligence that is being questioned here about whether or not these deals are providing enough disclosure so that investors can make an informed decision.

When you are targeting retail investors, which Reg A+ does, you need more involved disclosure. What has not been discussed today, and the reason large companies shouldn't be required to put disclosure—and it has been conventional wisdom in the capital markets for 70, 80, 90 years—is that you have the largest institutions who do the due diligence with people like Ms. Howe at their side. So, you don't need that level of disclosure or diligence because somebody is doing it.

There have only been a few hundred deals that have been done on Reg A+, and its average raise size is \$2.2 million, but we do not need to utilize it more and find a utility for it.

Mr. GARBARINO. And you think raising the cap could get more companies involved?

Mr. ELLENOFF. I spoke to several of the platform managers, and they agreed that there are times when they speak to some of the companies who feel that the \$75 million as a top limit makes it unattractive to them, so they won't do a deal on Reg A+.

Mr. GARBARINO. I have some more questions, but they are much more detailed—

Mr. ELLENOFF. Oh, one last thing, if I may?

Mr. GARBARINO. Sure.

Mr. ELLENOFF. It has not been discussed, and I am not really supposed to go here, but I think that if crypto was to become a regulated vehicle, as has been suggested by our regulator community, Reg A+ is the perfect onramp for it. So far, the regulators have not been accommodating for that conversation. But had they been, then \$75 million would definitely be utilized on a regular basis.

Mr. GARBARINO. Thank you. And I do have other questions about this, but I will have to send them to you.

I do want to ask you also about finders. Right now, there is no suitable framework for finders which, because of this, they are treated as broker-dealers by the SEC.

Is this a problematic framework for those seeking to make connections between investors and private companies? If so, can you expand upon that? And would changing this and creating a framework benefit rural and underserved areas?

Mr. ELLENOFF. Yes, yes, and yes. It has been sitting out there for 25 years and it is just getting fumbled all the time. And there is no good reason not to have finders be able to qualify under the old, "Paul Anka" sort of test or some expanded no-action letter like that.

Mr. GARBARINO. So, this is really affecting access to capital and we need to fix it?

Mr. ELLENOFF. Without question. Small businesses need people to help them identify appropriate investors.

Mr. GARBARINO. Thank you very much. I yield back, Madam Chairwoman.

Chairwoman WAGNER. The gentleman yields back.

I think we have completed our questioning time period. I would like to thank all of our witnesses for their testimony today. So much of it was just absolutely inspiring, and I thank each and every one of you, as does our committee.

The Chair notes that some Members may have additional questions for this panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 5 legislative days for Members to submit written questions to these witnesses and to place their responses in the record. Also, without objection, Members will have 5 legislative days to submit extraneous materials to the Chair for inclusion in the record.

The hearing is now adjourned.

[Whereupon, at 3:49 p.m., the hearing was adjourned.]



# **A P P E N D I X**

February 8, 2023

**Statement of McKeever E. Conwell, II  
Managing Partner, RareBreed Ventures  
before the U.S. House of Representatives Committee on Financial Services  
Subcommittee on Capital Markets  
“Empowering Entrepreneurs: Removing Barriers to Capital Access for Small Businesses”**

**February 8, 2023**

Madam Chair Wagner and Ranking Member Sherman, thank you for the opportunity to testify today on the importance of creating better access to capital and removing barriers for both entrepreneurs and those who fund their amazing companies. My name is McKeever E. Conwell, II, and I am the Founder and Managing Partner at RareBreed Ventures (RareBreed) which I am representing today. RareBreed is a venture capital (VC) firm that invests in, and supports, innovative product and technology startups in the earliest stages of their business that are in locations typically overlooked by the majority of other VCs.

I want to first say that I am here to address the much-needed Improving Capital Allocation for Newcomers (ICAN) Act due to my personal experience in raising a fund and my expertise. I want to also clearly state that I am in full support of all seven bills being addressed today as they all address removing barriers to capital access for small businesses.

**I am the American Dream**

I’m the son of an Air Force veteran who became a postal worker and a bank teller. I went to college at Morgan State University, a Historically Black College and University, where I studied Computer Science and got an internship at the National Security Agency. I later dropped out of college to pursue a career as a government contractor supporting the Department of Defence to do my part for our amazing nation. In 2010 I would go on to start my entrepreneurial journey by founding two startups, the first of which exited by the sale of its intellectual property to a Fortune 100 company. In 2016 I began working for the Maryland Technology Development Corporation (TEDCO). TEDCO is a Maryland economic development corporation that is also the largest funder of early-stage startups in Maryland by volume. It was at TEDCO that I learned to be an investor and led the creation of, what was at the time, the first state-backed pre-seed

fund specifically for founders typically underrepresented in the world of venture-funded startups, today known as the Builder Fund.

### **Lack of Access to Capital Is Holding Back Founders of Color and Our Country**

I launched RareBreed Ventures in late 2020 as a response to the lack of access to capital for founders of color and founders outside of the major investment hubs of Silicon Valley, New York, and Boston which account for 75% of all VC funding. As well as a response to the lack of cultural competency from many VCs when it came to investing in founders who didn't look like them or didn't come from a similar background.

### **A Real-World Example of How Lack of Access Manifest**

These two issues came to the forefront for me in the form of an amazing entrepreneur who is the inspiration behind me creating RareBreed Ventures. A few years ago I met an amazing founder named Shawna Stepp-Jones, a single mom from my hometown of Baltimore. She told me she wanted to create a tumble dryer that could dry a wig or hair extension in 15 minutes with no heat. As someone who grew up around women with wigs and hair extensions, I knew just how big of a problem this was. Even today most women still wash their wigs and hang them up to dry overnight at home or professionally<sup>1</sup> at salons. I immediately got what she was trying to create and the impact of such an innovation but other investors didn't. Keeping in mind Shawna has an engineering degree from Morgan State University and a Master's from Johns Hopkins University and at the time was a patent examiner. Even still I watched for 3 years as she get nothing but no's from many folks who didn't look like her until she decided that the only way for her to get access to capital was to become a surrogate mother. Even knowing that Black women are three times more likely to die from a pregnancy-related cause<sup>1</sup>. She was willing to take that risk in order to build a product that served her community and chase her dream.

### **How Being Creative with Current Regulations Got Us Here**

Shawna and founders like her are the reason I founded RareBreed Ventures but there was a problem. When I decided to start RareBreed, even though I knew how to invest from my time

---

<sup>1</sup> CDC – Office of Minority Health & Health Equity (OMHHE) – <https://www.cdc.gov/healthequity/features/maternal-mortality/index.html> April 6, 2022.

working for the state of Maryland, I didn't have a network of wealthy folks to raise the fund from. That caused me to get creative with how I source the people who would invest in my fund and how I would go about building the fund. To do this I used 2 regulations. First, was Rule 506(c) of Regulation D which allows for the public solicitation of a funds offering but required that every investor in that fund to be an accredited investor. The second was the amendment to section 3(c)(1) of the Investment Company Act of 1940 (15 U.S.C. 80a-3(c)(1)) which allows for a fund of \$10,000,000 or less to have up to 250 investors.

With the first regulations, I was able to use social media, Twitter mainly, to meet with many potential investors. Thanks to my growing profile as someone who helps startups and shares a lot of knowledge on venture capital I was able to have 1,128 meetings in my first 90 days of fundraising. Eventually, I would have more than 4,000 meetings over 18 months to fully raise RareBreed Fund I. The second regulation allowed me to start off fundraising by allowing investors to invest as little as \$10,000 compared to the \$100,000 minimum investments most funds would have to ask for before the amendment. This led me to have 194 investors in RareBreed Ventures fund I. Of those investors, 65% invested \$25,000 or less, and 83.5% of which invested \$50,000 or less. Many of these investors are people of color and or first-time investors in a fund because they had never had access to make such an investment or couldn't risk the high minimum threshold for a fund. Keeping in mind all of these investors are accredited and with means but still need to be prudent with their investments and capital. This means that before I offered them this opportunity in RareBreed they were limited to investing in companies either directly where there is a much higher risk of losing all of their money or, investing in stocks of publicly traded companies which the average VC funds have historically outperformed.

"As of June 2020 the VC funds raised from 2007 to 2016 in the Burgiss Manager Universe had outperformed the Russell 2000 (a small-cap index) by 7% a year, on average, and the S&P 500 by nearly 5% a year. Almost 75% of those funds had beaten the Russell 2000, and roughly 60% had beaten the S&P 500."<sup>2</sup>

---

<sup>2</sup> Paul Gompers, Will Gornall, Steven N. Kaplan, and Ilya A. Strebulaev. "How Venture Capitalists Make Decisions" (2021). Available at: <https://hbr.org/2021/03/how-venture-capitalists-make-decisions>

It has been incredible to see so many investors getting the opportunity to invest in this asset class. Now they are taking part in the engine that is generating wealth which they were once excluded from, and in many cases thanks to the work at RareBreed, helping drive innovation in the communities they care about.

#### **What Got Us Here Isn't Enough and Excludes Many**

This is such a great start but more is needed and that is why the Improving Capital Allocation for Newcomers (ICAN) Act is so important. Without the ICAN Act, almost all of those small dollar investors who make up 83.5% of the investors in RareBreed Ventures Fund I will not be able to invest in RareBreed Ventures fund II. That's 162 out of 194 investors. This is because RareBreed Ventures fund II has a goal of raising much more money, limiting us to 100 investors and forcing us to raise our minimum investment into the fund to \$100,000 - \$500,000 which is a far cry from the \$10,000 - \$50,000 from our first fund. Investors who are happy with the work RareBreed is doing and who would want to continue to invest in our fund will not be able to no matter how much they want to. Reducing the amount of money we could potentially raise for RareBreed's next fund.

The current rules basically price out many accredited investors from being able to participate in such an investment fund. Limiting the amount of capital and sources of capital for smaller and newer investment funds. Leading to less capital to help drive innovation, economic growth, and job creation. This is especially true when talking about companies started by founders of color because we know that in particular Black-led funds are four times more likely to invest in a Black-led company<sup>5</sup>. As an example, RareBreed Ventures does not have any diversity mandates for how we invest but of the 40 companies we have invested in to date 64% of our companies have an underrepresented founder, 44% of our companies have a founder of color, 38% of our companies have a Black founder, and 33% of our companies have a female founder. These numbers are far cries from the industry standards of less than 5% for each of those categories. Also keeping in mind that almost all of the Black-led venture funds in America

---

<sup>5</sup> Barrios, John Manuel and Hochberg, Yael V. "Taxing Carried Interest as Ordinary Income and the Potential Impact on New Venture Fund Formation" Nov. 2021. [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3939267](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3939267).  
Source: State of Black Venture Survey

would fit under the new rules in the ICAN Act because most of our funds are less than \$150,000,000.

#### **This Is Why We Need the ICAN Act**

With the ICAN Act, such limiting factors would be greatly reduced. First, this would allow accredited investors to not only have more opportunities to participate in the asset class of venture capital but also allow them to reduce their risk. With lower minimums for these newcomer funds, investors can now invest smaller amounts of money in more VC funds to spread out their risk and better diversify their investments. Secondly, this would allow investors to raise more capital in their early funds. Today many funds have to turn away investors who are willing to invest even more than \$100,000 because of the limit on the number of investors in a fund. This results in millions of dollars in potential funding for future innovation and job creation. While also, excluding these investors from being able to truly diversify their own investments and limiting their ability in wealth creation. While raising our first fund, we got enough interest to actually raise over \$30,000,000 but had to turn away most of it due to the limits of the current regulations. The idea that in a capitalist country where individuals who meet the accredited investor status are told they aren't able to make certain investments because they aren't wealthy enough seems wrong. Even more so, those who do have enough wealth to continue to participate in the venture asset class are almost exclusively from a non-diverse population. This only serves to further widen the racial and gender wealth gap in America and puts limits on the types of innovation we see in our country.

#### **Conclusion**

I am excited to see Congress working through issues that impact the access to capital that drive innovation. I appreciate that policymakers have to balance protecting the public from scammers and bad actors while reducing barriers to economic growth, job creation, and innovation to continue to make our country the best in the world. As someone who has spent my entire career in venture capital as an advocate for access to capital and reducing barriers, I look forward to being supportive and assisting this committee in any way possible. Thank you for this opportunity to testify today, I look forward to your questions.

Testimony

Before the U.S. House Committee on Financial Services

Subcommittee on Capital Markets

Hearing on “Empowering Entrepreneurs: Removing Barriers to Capital Access  
for Small Businesses”

Douglas Ellenoff

Partner, Ellenoff Grossman & Schole LLP

February 8, 2023

Good morning, Chairman Wagner and members of the Capital Markets subcommittee. It is a pleasure to be a part of this important hearing “Empowering Entrepreneurs: Removing Barriers to Capital Access for Small Businesses.” I was last before this subcommittee September 11, 2019 for the hearing: “Examining Private Market Exemptions as a Barrier to IPOs and Retail Investment.” There have been significant developments in the capital market since and we are now back to an environment where entrepreneurs need further assistance of Congress. I trust that you will seriously consider the Proposed Bills.

My name is Douglas Ellenoff. I am a partner at the New York based law firm of Ellenoff, Grossman & Schole. I am a corporate and securities lawyer and have been practicing for over 35 years. My law firm has been in business for more than 30 years and there are nearly 130 lawyers and we are regularly one of the top 10 IPO and finance law firms in the nation. We are market leaders in several alternative finance programs, including Crowdfunding, SPACs, PIPEs and Registered Directs.

I have spent nearly 10 years after the passage of the JOBS Act working with the leadership of the crowdfunding movement, traveling extensively domestically and abroad, including dozens of trips to DC, to provide our views on the proposed and final Regulation Crowdfunding and various JOBS Act rules and regulations.

I am counsel to the Association of Online Portals, the leading voice in DC for the industry and have had a prior association with the Crowdfunding Intermediary Regulatory Authority in a similar position.

I am a co-founder of LawCloud, and GUARDD, two legal technology companies catering to the broader crowdfunding industries.

My comments are those of my own and not my firm, nor my clients or the associations to which I am affiliated with.

Given today's volatile market conditions, where capital is scarce for entrepreneurs, not unlike the period right before an overwhelmingly bi-partisan Congressionally enacted JOBS Act, the timeliness of today's hearing is more important than it's been in the past decade.

According to the data published by Crowdfund Capital Advisors, from the period of inception of Regulation Crowdfunding to 2019 my last testimony here, there was \$193.8mm raised in the aggregate. Since 2019, until today \$1.4 billion has been raised. This 7x increase clearly demonstrates the commercial acceptance and viability of what Congress put in motion in 2012 with the JOBS Act. There have been over 4,300 funded transactions- 3,500 just since 2019. Importantly, the number of jobs created just from Crowdfunding and not the other provisions of the JOBS Act has been nearly 225,000. Although the studies are limited, the data indicates that of these funded transactions, 55% of them has at least one woman or minority founder, have an 81% success rate and represent nearly 47.8% of all capital raised. We can all be very pleased with the results of Crowdfunding, which would not have been implemented without the support of all constituents represented here. Regulators were decidedly uncomfortable with the idea of Crowdfunding and many of their stated concerns didn't materialize. Had we not proceeded and acted together, our economy wouldn't have benefited and, more importantly, those entrepreneurs wouldn't have been funded and been able to hire employees and execute their dreams and make them a reality. It's a wonderful example of Congress taking action that has very positive real-world impact.

On a personal note, since my last testimony, my fellow panelist Renee Jones left her professorship at Boston College Law School to be appointed Director of the Division of Corporation Finance of the Securities and Exchange Commission, and Mike Piecek finished his time as head of the Department of Financial Regulation of the State of Vermont to be elected as the State's Treasurer, so as you might suspect, I am a little disappointed that my status remains unchanged but I remain hopeful that my testimony here may have a similar impact on my professional resume as it has for my esteemed colleagues.

I look forward to sharing my views on many of the proposals that will be discussed at today's hearing and thank Chairman McHenry for hosting this important hearing today.

## **INTRODUCTION**

Similar to most industrialized nations, the presumption contained in our securities laws is the requirement that any offer and sale of securities must be registered with the Securities and Exchange Commission (SEC). The underlying notion is that the public at large generally needs some protection from bad actors and that full and fair disclosure (i.e., a true and accurate description of the business, its management, the capital structure, financial status of the operations and the associated risks) will be provided to them prior to an investment in order to enable all investors to make an informed investment decision. Our federal securities laws, as opposed to certain of our states, premise our statutes on the thoroughness of the disclosure of

each issuer and not the merits of the investment. Since the enactment of the Securities Act of 1933 and its related provisions in the Securities Exchange Act of 1934, which requires ongoing and updated disclosure by registrants to facilitate secondary trading, it is fair to say that this regime has been the foundation for the most active liquid securities market in the world. Our securities laws are the basis for many other jurisdictions and are regularly monitored by other governments and regulators to assist in informing their own continuing positions with respect to new innovations and reforms. We too should be mindful of what these other jurisdictions are seeking to accomplish, since they are competing with us to attract companies to raise capital more efficiently and retain these companies for secondary trading. This is why it continues to be important to analyze what is working with our capital markets and what isn't or is achievable in new methods with the introduction of new technologies. While I am not an expert in the securities laws of many of the other competitive jurisdictions, it seems unquestionable to me that based upon many experiences we have had with cross-border transactions and alternative finance programs, that our business enterprises are required to operate in the most complex series of intertwining rules and regulations.

The positive result generally is that our markets are trusted and attract capital from around the world. There are negatives though that should not be lost or ignored simply because our overall formula for market structure and governance has been unarguably successful. Is the cost of being public too burdensome? Yes. Compliance costs are resulting in companies remaining private substantially longer than previously. Although off topic from today's proposals, how is it ok that before SEC proxies by a company in a public merger, the plaintiff's bar is already lining up to claim that there have been deficiencies in the process? It is simply unseemly. It makes sense episodically to analyze where we are in the regulatory cycle and ask whether we are being too lenient or too restrictive. Like many complex issues, there is no easy answer and it may depend upon where you are looking—in the public markets or the private. Unquestionably, the current regulatory environment is unkind to being either a public company or a private company. There is a culture of regulation by enforcement, as well as, the convenient re-interpretation of rules and regulations that have been on the books for years and years.

Compliance is unquestionably complex and, in many cases, unclear. While regulators generally are available to provide guidance on how to proceed in a manner that they are comfortable with, there is inconsistency at times, even subjectivity to prohibit activity that it would appear they are uncomfortable with. Much of it is just human nature but does create tension in the system and give pause to businesses that are considering being public in the U.S., or remaining public. At this time, I would however note that in our experience, much of the confusion seems by institutional intention and not by individual choice. In a global market, we need to recognize that our securities laws and how they are interpreted are being assessed around the world to determine if we are a hospitable and beneficial place to entrust their capital formation and trading.

We are here today to consider proposals for improving our capital markets. I will argue that some enhance our standing in a meaningful manner and others are merely incrementally

attractive. Please consider that as a securities practitioner who respects the efforts of all securities regulators and their daily tasks of protecting investors from the opportunism of bad actors, who are either expedient in their approaches without regards to the effects on others or outright wrongdoers, I am very sensitive to the SEC's charter of continually seeking the proper balance between capital formation in both the private and public markets, even though I would observe that the current zeitgeist believes that it is decidedly more investor protective and more antagonistic to investing and capital formation.

### **EXEMPTIONS**

It has always been acknowledged by Congress and the SEC since the beginning of our Federal securities laws that not all securities offerings must be, or even should be, registered and reviewed by the SEC.

The statutory inclusion of exemptions from registration with the SEC, is an acknowledgment by both Congress and the SEC that there are certain investors that don't need the protections that other less sophisticated and more vulnerable investors may require.

Presumed in these exemptions is the notion that those investors have the ability to make their own informed decisions, perform due diligence, value the companies being considered and structure the financings as appropriate. The benefit of being in this category of investors, albeit whether one is an individual accredited investor or an institutional investor that meets one of the exempted investor category status, is that the private enterprise seeking the necessary funding will not have to subject themselves to the financial, regulatory and administrative burdens of having to register with the SEC.

Being an investment opportunity that can access the private markets is of significant advantage because it saves the time, resources and expense of having to register and comply with the very complex securities disclosure laws and PCAOB financial statement requirements, among other regulatory costs.

Mind you, neither registering nor being exempt changes the risk profile or investment character of the investment. I would like to emphasize that just because an enterprise is prepared to register their securities and comply with the SEC registration process doesn't makes them a better investment or less risky. The point of registration in my judgment is that we collectively have decided that full and fair disclosure is necessary and important to protect unaccredited retail investors from making an uninformed investment decision.

Registration doesn't ensure a successful investment, just relevant information. Since investors in exempt offerings are presumed to be able to protect themselves and not require those protections, a private market has always been in active existence and is substantially larger than our public markets. This is a good thing and the venture markets and real estate markets are but a couple of examples of how private entrepreneurship has flourished free from the burdens of registration with a statistically tolerable amount of fraud and litigation profile. To be clear, however, no amount of fraud is acceptable, and we should and have laws in place to

penalize those that act outside of the bounds. Unfortunately, just because there is the reality of fraud shouldn't deter capital formation and capital markets advances. Crowdfunding is another wonderful example of a private market exemption balancing proper disclosure and investor protection in a new manner that was previously not permissible.

Are there failures as well as successes? Absolutely. However, we as a collective society are supportive of that subset of the private markets because it doesn't harm individuals that aren't arguably able to bear the risk of those losses. From a practical matter at this point, it would seem unrealistic to me that the existing SEC would even be equipped, much less want, to assume the burden of the tens of thousands of private enterprises that avail themselves of the exempt markets and have raised investor funds.

### **EXPANDING THE PRIVATE MARKET IN A CONTROLLED AND RESPONSIBLE MANNER**

The various JOBS Act provisions that Congress enacted (to its credit) back in 2012 have been beneficial for retail investors while maintaining the appropriate balance between capital formation and investor protection. Notwithstanding a remarkable amount of outspoken investor protection advocacy to the build-up of the passage of the JOBS Act, Title III Regulation Crowdfunding in particular, it is now commonly acknowledged by regulators that none of the doom and gloom prognostications of fraud or litigation has presented itself. It is unlikely that fraud won't occur in the Regulation Crowdfunding space, but many of the stated reasons for frustrating this quite novel exemption haven't presented themselves yet.

There is no doubt there have been investor losses (as well as profits), but yet no meaningful investor upset spilling into the complaint lines of the SEC, FINRA or the state regulators. I believe the reason is that so far retail investor through advanced technology solutions has ensured that they be educated about the risks of Crowdfunding generally, as well as being provided all the necessary business and financial disclosure, as well as, advising them of the associated risks. The digital footprint for recording the full transparency of the process also keeps both sides compliant.

The funding platforms and issuers have properly educated their investors and provided them with limited scaled down legal and financial disclosure in a readable and digestible manner. I am often asked why Regulation CF has only funded a little less than a thousand companies and raised less than a few hundred million dollars. My response has been both that all new programs take a considerable amount of time in my experience to develop if you want them to grow organically and responsibly. And secondly, and more importantly, if the size of the market is the primary issue of concern now and not that the experience of this exemption hasn't actually caused severe regulatory backlash, then we should all sigh a big relief that we have bench tested the program and it is working successfully. Potential for fraud was one of the primary reasons that Congress reduced the maximum amount that companies could raise and in this light it should be reconsidered. Now that such fear hasn't been substantiated, we should take this opportunity to explore making some improvements, and taking off or relaxing some of

the guardrails of regulation. My observation would be to take a victory lap on this bipartisan initiative, and reflect on what changes are necessary for greater impact. The few thousand entrepreneurs have been funded, several hundred thousand jobs is a good start!

More businesses and jobs would be created, more geographically diverse enterprises would be funded, and more entrepreneurial opportunities started by more minorities and women would access capital. We thought this ultimately would be the outcome of Regulation CF – and this was a key rationale in advocating for it. Now that these positive outcomes have come to pass, key additional reforms would fully leverage these early successes.

This is also true of Title II General Solicitation and Regulation A+. I think General Solicitation speaks for its success. Regulation A+ on the other hand needs to still find its footing.

My sincerest emphasis and admonition though for you today, as you consider additional changes and additions to the JOBS Act provisions and other private market proposals, is to remember that Congress took bold bipartisan action in 2012 against much antagonism from regulatory adversaries of the legislation. Many of those concerns as stated at that time have not materialized. We have enough information to know that much more good can come by enhancing the sound bipartisan legislation that passed in 2012.

With respect to the 4 proposals to be considered at today's hearings, please find my views and thoughts below:

**1. H.R. \_\_\_- "To amend the Securities Act of 1933 to preempt state securities law requiring registration for secondary transactions."**

Otherwise referred to as "Improving the Crowdfunding Opportunities Act", this proposal seeks to further enhance the secondary trading of the securities purchased by investors. This proposal is similar to the treatment that publicly-traded securities receive pursuant to the National Securities Markets Improvement Act of 1996, whereby Congress facilitated the pre-emption of state securities regulation for those securities publicly-listed and traded on either NYSE/AMEX or NASDAQ. Practically, this would enable investors to obtain greater liquidity for their already-held positions and improve the attractiveness of crowdfunding and other private market exemptions. To the extent that tokens are encouraged to be treated as securities offerings by regulators, this improvement would be one less reason for those issuers to remain non-compliant.

For the stated reasons, and others, I would encourage the approval of this proposal.

**2 H.R. \_\_\_- "To amend the Securities Act of 1933 to provide small issuers with a micro-offering exemption free of mandated disclosures or offering filings."**

Otherwise referred to as the "SEED Act of 2021", this proposal seeks to further enhance private exemptions and make it substantially easier for start-ups and small business to raise capital.

The proposal would relieve issuers from the substantial disclosure and filing burdens imposed by other offering exemptions, but, remain subject to the anti-fraud and “bad boy” disqualifications. As we all observed during the Covid lock-downs, small businesses and restaurants suffered immeasurably. Had this exemption been in place, those entrepreneurs may have had an easier time raising capital from their customers and avoided liquidation or going out of business. Raising capital in the amount of \$250,000 or less is not currently cost effective given the compliance issues. H.R. 5458 seeks to redress this marketplace friction.

For the stated reasons, and others, I would encourage the approval of this proposal.

**3. H.R. \_\_\_- “To amend the Securities Exchange Act of 1934 to create a safe harbor for finders and private placement brokers.”**

Otherwise referred to as the “Unlocking Capital for Small Businesses Act of 2022”, this proposal seeks to finally codify one of the longest lasting proposals floating in the securities industry that would enhance private market activity and make it easier for start-ups and small business to work with member accepted finders to facilitate and assist in the capital raising process. As SEC Commissioner Roisman wrote in his October 2020 remarks on this proposal, “for almost fifty years, finders have approached the staff regarding whether a particular activity or business model would require broker registration.” He also highlighted that “in 2005, the ABA Task Force on Private Placement Broker-Dealers recommended that the SEC work with FINRA and state regulators to establish a simplified system that would allow persons to solicit investors for small issuers, subject to a reduced but appropriate , level of regulations.” As he then points out “The lack of clarity regarding the status of finders has had detrimental effects for issuers and investors.” Commission Roisman is joined by many other securities law professionals that believe it is high time to finally address this lingering issue and benefit our small business community.

For the stated reasons, and others, I would encourage the approval of this proposal.

**4. H.R. \_\_\_- “To require the Securities and Exchange Commission to revise rules relating to general solicitation or general advertising to allow for presentations or other communication made by or on behalf of an issuer at certain events.”**

Otherwise referred to as the “Helping Angels Lead Out Startups Act of 2022” or the “HALOS Act of 2022”, this proposal seeks to finally codify another ongoing debate about how to comply with certain of the private offering exemptions and be able to disseminate presentations and other communications at certain events, particularly Angel Investor Groups, a defined term, which may only be comprised of Accredited Investors, who meet regularly, without running

afoul of the general solicitation or general advertising rules. This proposal is seeking to clarify that certain routine activity used by an issuer in its fund raising process, to a defined audience, will not cause such issuer to have to comply with the more onerous provisions of 506c and have to verify the accreditation of all the participating investors. H.R. 9451 recognizes that Angel Investor Groups by their very nature are sophisticated investors with net worths that don't require regulatory protections in this manner and without this proposal the securities law are unnecessarily preventing the issuer from using the Angel Investor Group forum efficiently and providing them with more detailed information and presentation. This frustrates the capital formation process.

For the stated reasons, and others, I would encourage the approval of this proposal.

Testimony before the U.S. House Financial Services Committee  
Subcommittee on Investor Protection, Entrepreneurship and Capital Markets

**“Empowering Entrepreneurs: Removing Barriers to Capital Access for Small  
Businesses”**

Deborah Gladney  
CEO and Co-Founder, Worktorch

February 8, 2023

Chairman Wagner, Ranking Member Sherman, Ranking Member Waters, and members of the Subcommittee, thank you for the opportunity to appear here today.

My name is Deborah Gladney and I'm the CEO and co-founder of Worktorch - a career platform for service workers based in the heartland of Wichita, Kansas. I'm honored to be here today with my sister and cofounder Angela Muhwezi-Hall and be present for such a critical agenda that impacts entrepreneurs like us from across the country.

When we started our company at the peak of the pandemic, we had no idea our company would take us to the places we've been, help the people we have helped or allow us to see the things we have seen. Things such as the extreme disparities in access to resources and capital amongst entrepreneurs.

Last year, startups with all-women founding teams like ours received just 1.9% of all venture dollars. And for black founders, we received just a mere 1%.

As if the odds aren't stacked up against us enough - 75% of all venture capital investments go to just three metro areas. And I can promise you, Wichita isn't one of them.

According to the data - my sister and I - as black women founders in Kansas, should not be here in front of you today.

What made the difference you may ask?

We had our first example of hard work from our parents. They came to this country from Uganda and worked hard to obtain their doctorate degrees all while raising their five children with no support or generational infrastructure built in this country. They were our first example of what it means to be an entrepreneur - to build something out of nothing. To be scrappy and resilient, even if you're told no 100 times a day. To take risks, even if it means leaving what feels comfortable, for the chance at building something big.

Even if it means me walking away from a six-figure salary while 8 months pregnant to build Worktorch. Even if it means my sister leaving an esteemed university in beautiful L.A. to live in

my basement with her husband as we built our company. We did it because we knew building Worktorch not only had the power to change our lives, but the lives of service workers and their families. Everyday, our company helps people find fulfillment in life while being rewarded for what they do.

But without our parents' example, I don't think my sister and I would have made it this far.

When we started Worktorch - we had no connections, or friends and family we could lean on for capital. We cold pitched 379 investors. And received 379 no's. We had to pull money from our own 401Ks to build our product. But with our little money, we created a platform that garnered over 1,000 users in the first few weeks without receiving a dollar from anyone else.

The scrappiness our parents taught us is what got us to the point of eventually becoming the first black women in Kansas to raise over \$1M in venture funding. But we also came to the table with twice as much - often to get twice as less.

It's also hard for us to be proud of the fact that in 2023, we are still seeing a lot of firsts for minority and rural entrepreneurs. Access to capital is literally stunting the ability for many businesses like ours to grow.

And this is why today's proposed bills are so important.

Wouldn't it be great if more people who looked like me could invest in people who look like me? As a nation, we know the benefits of encouraging entrepreneurship across backgrounds: we create jobs, spark innovation and allow America to maintain its position as the most competitive nation on the planet.

It's in our nation's best interest to foster more firsts like my sister and I, and create more seconds, thirds, fourths and beyond... to where we won't even have to count anymore.

It's my hope you'll be on the right side of entrepreneurial history today. Thank you and I look forward to your questions.



Empowering Entrepreneurs: Removing Barriers to Capital Access for Small Businesses  
 Capital Markets subcommittee  
 US House of Representatives  
 Committee on Financial Services

Darcy A. Howe  
 Founder, Manager Director  
 KCRise Fund

Wednesday, February 8, 2023

**What is wrong with the world that we need these seven bills?**

Chair Wagner, Ranking Member Sherman and Distinguished Members of the Subcommittee on Capital Markets, I'm Darcy Howe from America's Heartland, Kansas City, and I've seen barriers to capital access firsthand.

75% of venture capital to invest in technology startups comes from three states: California, New York and Massachusetts. There are bold, innovative ideas to solve business and societal challenges in every county in this country that have gone unfunded and that was a contributor to slow economic growth in my region.

In 2015, KC business leaders realized that after the 2008 downturn, we did not bounce back as well as peer cities such as Indianapolis and Nashville. Many set out to bring solutions to the region, and my volunteer assignment was to understand what was happening in entrepreneurship.

What I learned was 70% of all net new jobs in the KC region came from someone starting a business, but those starting high growth technology companies were leaving the area because capital was on the Coasts. Further, I learned that most rural entrepreneurs, people of color, and women were not getting funded at all.

**What did we do to bring inclusive capital to Kansas City?**

With friends, we started an angel investing group to invest in women-led businesses, Women's Capital Connection. Then, I decided to retire from a successful 32 year career as a wealth manager and devote these past six years to raising capital and funding amazing innovators in the region through KCRise Fund.

Illustrating success when capital and innovators are connected, in six years, the 46 portfolio companies in our fund have created more than 1000 jobs with an average wage of \$98,000. If our 46 new companies were one company, we would now be the 40th largest company in the region.

In the past three years, 62% of our investments included at least one founder from at least one underrepresented demographic. 51% of the employees of our portfolio companies come from an

underrepresented demographic. These inclusive statistics far exceed Coastal venture-backed businesses.

You have now met one of our amazing founders, Deborah Gladney, and can see why investing in WorkTorch was not a hard decision for my partners and I. KCRise Fund invested \$400,000 and made introductions to venture capital in other parts of the country which lead to 4 more firms investing for a total of \$1.1million. As the eyes and ears of our region for VCs around the US, our support was validating to other VCs in our network which made her raise successful.

**So tell me again, why we need these seven bills?**

While I can speak to the DEAL Act, SEED, HALOS and ICAN, ICAN is the bill which would unlock the most access to capital for small venture funds like KCRise Fund, and on which I will focus my remaining remarks.

Our first fund was \$19 million and it took me two years to raise! Limited to 99 accredited investors, I had to find people willing and had the resources to invest nearly \$200,000. For Fund II we wanted to increase capital to the region, so set out to raise \$40million which meant the average investor had to commit \$400,000. Not every small venture fund manager has the network I had built over 30 years and even I had trouble raising for startups, a type of investment that most people had never invested in before.

Please don't confuse us with the big-time private equity bunch with mountains of money. There are 100s of small funds like ours springing up in smaller markets and we all would benefit from raising the limit on total number of investors. It would accomplish three things: First it would allow more folks to participate. Funds could take investors at much lower levels such as \$10,000 or \$50,000, increasing access for small investors. Secondly, by being able to take more investors, we can more easily build a larger fund, bringing increased capital to our market. And finally, a business reason to attract more people to start a small venture fund. Fund administration, tax prep, audit, legal, rent, investor communication, events and fund management all take capital. Seeing a path to building a fund which can pay for all of these things and build a small team to help the entrepreneurs will increase access to capital as more funds are formed.

**On behalf of small fund managers, angel investors and startups, appreciation for your focus on this high growth sector of our economy!**

More inclusive capital is the lifeblood of new jobs in counties all over this country. We are seeing already, in our region that generational prosperity is broadening due to our focus and increased capital.

Thank you for this opportunity to represent small investors and small fund managers who will benefit from your thoughtful improvements in policy.

**Written Testimony of**  
**Alexandra Thornton, Senior Director**  
**Center for American Progress**  
**Before the United States House of Representatives Financial Services Committee**  
**Subcommittee on Capital Markets**  
**“Empowering Entrepreneurs: Removing Barriers to Capital Access for Small Businesses”**  
**February 8, 2023, 2pm**

Chairwoman Wagner, Ranking Member Sherman, and esteemed members of the subcommittee, thank you for the opportunity to appear before you today to discuss capital access for entrepreneurs and small businesses.

My name is Alexandra Thornton. I am a senior director focusing on financial regulation and tax policy at the Center for American Progress, an independent, nonpartisan policy institute that is dedicated to improving the lives of all Americans through bold, progressive ideas, as well as strong leadership and concerted action.

Entrepreneurs and small businesses have been an important part of the American success story from our country’s beginning. As SEC Commissioner Caroline Crenshaw said last week, small businesses “form the backbone of communities, are drivers of jobs, are critical for the development of new ideas and new technology, and are an avenue to wealth creation...”<sup>1</sup>

---

<sup>1</sup> Commissioner Caroline A. Crenshaw, “Big ‘Issues’ in the Small Business Safe Harbor: Remarks at the 50<sup>th</sup> Annual Securities Regulation Institute,” U.S. Securities and Exchange Commission, January 30, 2023, available at <https://www.sec.gov/news/speech/crenshaw-remarks-securities-regulation-institute-013023>.

Entrepreneurs and small businesses make an enormous contribution to the innovation and creativity that America is known for, and they benefit a great deal from our capital markets. They could play an even bigger role in our economy, but lack of funding from the capital markets is not what is holding them back.

The simple reality is that, if a small business wants to get a loan, it has to go to a bank and fill out detailed loan application documents with information about its assets, projected finances, operations, and more. Its executives may have to offer meaningful collateral, such as their homes or their essential equipment and inventories. Those business loans are considered by the banks and their regulators to be among the riskiest activities in banking. Thus, they are subject to significant regulatory limitations, reviews, and compliance processes. For example, federal banking regulators frequently release guidance and notices intended to inform banks' risk management in lending to small businesses.<sup>2</sup>

By contrast, if a company wants to turn to the capital markets to raise capital, there may be no substantive, regulatorily imposed requirements at all. Today, after decades of deregulation, a company can raise an unlimited amount of money from an unlimited number of "sophisticated" investors without making any disclosures at all. As the SEC itself explained in 2019, "[I]ssuers in [Rule 506] offerings are not required to provide any substantive disclosure and are permitted to sell securities to an unlimited number of accredited investors with no limit on the amount of money that can be raised from each investor or in total."<sup>3</sup>

---

<sup>2</sup> See, e.g., Small Business Administration Lending Risk Management Principles, Office of the Comptroller of the Currency, OCC Bulletin 2021-34, available at <https://www.occ.gov/news-issuances/bulletins/2021/bulletin-2021-34a.pdf>.

<sup>3</sup> "Concept Release on Harmonization of Securities Offering Exemptions," U.S. Securities and Exchange Commission, 84 Fed. Reg. 30460, 30470, June 26, 2019, available at <https://www.govinfo.gov/content/pkg/FR-2019-06-26/pdf/2019-13255.pdf>.

Unlike banks and their employees, private equity and venture capital investors are generally not expected to follow regulator-mandated, standardized documentation requirements (and regulatory oversight) of their capital allocation decision making. This has become a hot issue, as the SEC is reportedly examining some venture fund investors' practices for potentially unreasonably overfunding private companies. This suggests that the capital markets may be giving private companies and funds too much money.

It is worth noting that small companies can also raise money through leveraged loans that are packaged into collateralized products—a practice that has been institutionalized in private equity and hedge funds and grown exponentially to trillions of dollars today.<sup>4</sup>

Venture capital and private equity funds are larger than at any time in history, and they also have more cash-like reserves on hand than at any time in history. This has created what has essentially become a sellers' market for many private issuers – and led to a deterioration in due diligence by many investors and ever rising private market valuations.

The problem is not that the rules prevent small businesses from obtaining capital; it is that the rules today allow companies with billion-dollar valuations, billions in revenues, and thousands of investors to never provide basic information to investors, regulators, or the public, and private funds to raise billions of dollars from underlying investors without basic expectations like timely, comprehensive, and reliable disclosures about their finances, governance, or operations. There is no regulatory requirement for these billion-dollar enterprises to provide investors with basic audits.

---

<sup>4</sup> See, e.g., "A Giant in the Shadows: Subprime Corporate Debt," Americans for Financial Reform Education Fund, January 2023, available at <https://ourfinancialsecurity.org/wp-content/uploads/2023/01/1.6.23-Subprime-Corporate-Debt-A-Giant-in-the-Shadows.pdf>.

Congress and the SEC created this perverse regulatory regime in the name of capital formation. Yet, as we have seen with Theranos, WeWork, and so many others, the current capital markets regulatory regime enables capital distortion. The regime does so in various ways, such as inflated valuations, lax internal controls, inconsistent disclosures across investors, and potential fraud and abuse.<sup>5</sup>

When Congress established the federal securities laws and created the Securities and Exchange Commission to implement them, it was responding to the massive investor losses and waste of the Great Crash of 1929. Congress was concerned that, without basic information about a company's finances, governance, and operations, capital would be mis-allocated and wasted. The fundamental bargain then and now is that companies that want to raise capital from the public must first provide basic information to investors and the public, including the company's financials, governance, operations, and risks. Today, public companies even need to be audited, and their auditors are subject to significant regulatory oversight. These robust audits are essential to promoting the integrity of the companies and the markets in which they operate. This disclosure of information improves price discovery, makes the markets more fair, more orderly, and more efficient, and protects investors from abuses, such as information asymmetry. Even the most sophisticated investors cannot exercise their superior knowledge and expertise if they do not have reliable information about a company's financials, operations, and risks – a lesson that, sadly, has had to be re-learned with great frequency.

When the securities laws were first adopted, and in the decades thereafter, offerings to even a single person or to a small number of employees were deemed to be public offerings in need of being registered. Congress and the SEC have since reversed those decisions, with increasingly alarming results.

---

<sup>5</sup> Crenshaw, January 30, 2023.

Beginning in 1982 with the promulgation of Regulation D, there has been a proliferation of exemptions from the public disclosure framework.<sup>6</sup> The stated intention of those exemptions and their subsequent expansions has been to provide more access to capital for small businesses.<sup>7</sup> But the reality is that those exemptions, along with a couple of loopholes in the law, have enabled virtually any company of any size to obtain capital from the public without complying with the public disclosure framework.

As a result, a substantial and growing number of companies are choosing to remain private as they raise capital, and often only end up coming to the public markets to cash out significant investors or founders. The result of Congress and the SEC creating and expanding exemptions from the federal regulatory disclosure framework is that the vast majority of capital raised is exempt. That explosive growth of the private markets has come at the expense of public markets.<sup>8</sup>

If a company can raise all the capital it needs in the private markets without making disclosures, developing robust operational safeguards, subjecting itself to audits, having a headquarters, dealing with a large number of retail investors, exposing details of its sales or operations to its competitors, suppliers, customers, or other business partners, or subjecting itself to SEC oversight and potential class action plaintiffs, why would it go public?<sup>9</sup>

The situation is truly alarming. Today, there are more than 650 U.S. private companies worth more than a billion dollars each in the U.S. private markets.<sup>10</sup> The number is going up every year.<sup>11</sup> Commissioner

---

<sup>6</sup> Elisabeth De Fontenay, "The Deregulation of Private Capital and the Decline of the Public Company," *Hastings Law Journal*, Vol. 68:445, 2017, available at [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2951158](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2951158).

<sup>7</sup> Crenshaw, January 30, 2023.

<sup>8</sup> George S. Georgiev, "The Breakdown of the Public-Private Divide in Securities Law: Causes, Consequences, and Reforms," Emory University School of Law, Fall 2021, available at <https://scholarlycommons.law.emory.edu/cgi/viewcontent.cgi?article=1001&context=faculty-articles>.

<sup>9</sup> See, e.g., "In the Public Interest," Healthy Markets Association, January 2022, available at <https://healthymarkets.org/product/public-vs-private-markets-a-special-report>.

<sup>10</sup> CB Insights, The Complete List of Unicorn Companies, available at <https://www.cbinsights.com/research-unicorn-companies>.

<sup>11</sup> Georgiev, 2021.

Crenshaw pointed out that these “unicorns,” as they are called, “have consistently relied on Rule 506 of Reg D to raise billions of dollars in U.S. capital.”<sup>12</sup> These companies are allowed to grow extremely large, competing with similar publicly traded companies and selling products and services to a broad swath of the American public, without making meaningful disclosures. As the recent examples of large, opaque company failures demonstrate,<sup>13</sup> these companies can pose huge risks to their investors, the economy, and the country. They do not belong in the private markets.

Rather than enabling small businesses to access needed private capital, Regulation D and other exemptions are being used by companies of all sizes to skirt the disclosure requirements Congress established to ensure transparency and investor protection. There are many steps that Congress and the SEC can take to rebalance the public and private markets and make more room for capital for small businesses.

Section 12g of the Securities and Exchange Act of 1934<sup>14</sup> was intended to prevent companies from becoming too large without adhering to the public disclosure framework. Originally enacted in 1964, it required expanded disclosures when a private company reached 500 holders of record, which the JOBS Act of 2012 increased to 2,000. When 12g was enacted, the number of holders of record was closer to the number of actual owners of shares. But now, due mainly to changes in technology, the holder of record definition is exponentially larger since intermediaries today may hold millions of shares *on behalf of* thousands of investors yet are counted as one holder of record for purposes of the threshold. This is why Facebook was able to remain a private company and avoid public disclosures for years after it had

---

<sup>12</sup> Crenshaw, January 30, 2023.

<sup>13</sup> See, e.g., Gillian Tan, Liana Baker, and Michelle Davis, “WeWork Postpones Long-Awaited IPO, Sending Its Bonds Falling,” Bloomberg, September 16, 2019, available at <https://www.bloomberg.com/news/articles/2019-09-16/wework-is-said-to-likely-delay-ipo-after-valuation-plummets?srnd=premium&sref=SSRP&RP>; and Zaw Thiha Tun, “Theranos: A Fallen Unicorn,” Investopedia, January 4, 2022, available at <https://www.investopedia.com/articles/investing/020116/theranos-fallen-unicorn.asp>.

<sup>14</sup> 17 CFR Section 240.12g-1.

thousands of shareholders.<sup>15</sup> Clarifying that “holder of record” under Section 12g means actual security owners or beneficial owners, not intermediaries, would help ensure that smaller businesses are not competing for capital in the private markets with huge companies.

A critical companion measure would be for Congress to statutorily require all very large companies and funds to be public. These companies and funds may have significant impacts on investors, but also markets overall and commerce generally. For example, there should be no such thing as a unicorn. Companies with billion-dollar valuations should be required to make basic public disclosures of their finances, governance, and operations, as should companies with more than 250 employees.

Beyond that, instead of trying to expand exemptions that are currently being used by much larger companies, Congress could do more for small businesses by scaling back the exemptions to their intended purpose, possibly eliminating some of them altogether, and by building on the success of the public markets with their mandatory disclosures. In this way, businesses would be more fairly competing for investors’ capital, as well as more fairly competing against one another.

Together, these measures would go a long way toward restoring the private markets to the businesses and investors they were intended for, while ensuring that larger companies that raise capital from the public comply with the public disclosure framework and thus provide the information those investors need to make investment decisions.

Thank you again for inviting me to testify today. I look forward to answering your questions.

---

<sup>15</sup> Steven Davidoff Solomon, “Facebook May Be Forced to Go Public Amid Market Gloom,” *New York Times*, November 29, 2011, available at <https://archive.nytimes.com/dealbook.nytimes.com/2011/11/29/facebook-may-be-forced-to-go-public-amid-market-gloom/>.

**Chairman Wagner question for Deborah Gladney**

- I. You mentioned in your testimony that, according to Pitchbook data, “less than 1% of all venture capital goes to rural startups.” This data is concerning. Small businesses and entrepreneurs, especially those from geographic regions and backgrounds that struggle to raise capital, cannot afford additional, unnecessary regulatory barriers. Instead, they need viable options and opportunities to raise capital. Many of the policies considered at the hearing provide exactly that. As the founder of a rural startup, can you explain how companies like yours would benefit from easier access to capital?

Although we have evolved so much as a society, access to capital is still a huge barrier for entrepreneurs like us... entrepreneurs from marginalized backgrounds or smaller countries and cities. Lack of access to capital is stunting the ability for many businesses to grow. And the current financial environment has placed an even greater burden on entrepreneurs like us who are trying to keep their businesses thriving in today's economy. Easier access to capital for entrepreneurs like myself means the creation of new products and services, new employment, and ultimately, the acceleration of our country's economic development.

- a. Would you hire more employees?
  - i. Yes. Hiring more employees would allow us to build and grow faster. Many of our competitors have been able to grow faster and obtain more market share because they were better funded.
- b. Would you have a greater impact on your community?
  - i. Yes. We're always asked, as a tech company, why we are based in Wichita, Kansas. We purposely choose to continue to build here because we believe it's our purpose to improve the lives of people around us - especially in our community. Every role we hire for, we always aim to hire locally first before looking remote. Because of this, six out of our ten employees are in Wichita.



February 8, 2023

The Honorable Patrick McHenry  
Chair  
House Committee on Financial Services  
2129 Rayburn House Office Building  
Washington, D.C. 20515

The Honorable Maxine Waters  
Ranking Member  
House Committee on Financial Services  
2221 Rayburn House Office Building  
Washington, D.C. 20515

The Honorable Ann Wagner  
Chair  
Subcommittee on Capital Markets  
2350 Rayburn House Office Building  
Washington, D.C. 20515

The Honorable Brad Sherman  
Ranking Member  
Subcommittee on Capital Markets  
2181 Rayburn House Office Building  
Washington, D.C. 20515

Dear Chair McHenry, Ranking Member Waters, Subcommittee Chair Wagner, and  
Subcommittee Ranking Member Sherman,

On behalf of our nation's venture capital (VC) investors and the entrepreneurs they support, thank you for holding the Subcommittee on Capital Markets February 8<sup>th</sup> hearing entitled "Empowering Entrepreneurs: Removing Barriers to Capital Access for Small Businesses." NVCA appreciates the committee's focus on finding legislative solutions to facilitate capital formation, expand entrepreneurial activity into more regions of the country, and support the next generation of high growth companies.

In particular, NVCA is thrilled to see the *Developing and Empowering our Aspiring Leaders (DEAL) Act* included as part of the hearing discussion, a longtime legislative priority that will improve capital formation in the earliest stages of the startup ecosystem. The *DEAL Act* will allow VC funds to acquire more shares from founders, angel, and seed stage investors and provide capital to emerging VC funds without triggering the costs and burdens of fund registration, providing liquidity and improving returns in the earliest stages of the startup ecosystem. These early-stage investors will then be able to make new investments into the next generation of nascent American companies.

NVCA is grateful for the exemption provided by statute that was intended to exempt venture capital funds from the costs and challenges associated with the Registered Investment Advisor (RIA) registration requirements imposed under Dodd-Frank. However, industry trends have made the definition of a venture capital fund promulgated by the Securities and Exchange Commission (SEC) in rule 203(l)-1 of the Investment Advisers Act in 2011 increasingly out of touch with the realities of today's startup ecosystem. The definition leaves out critical

participants in the entrepreneurial ecosystem, constrains the investment activity of some Exempt Reporting Advisors (ERAs) who must monitor investment strategies to actively avoid the regulatory morass of registration, and imposes unnecessary compliance burdens on other firms who participate in venture capital.

The *DEAL Act* is the legislative solution to this challenge. The bill would encourage capital formation for startups by directing the SEC to make a larger percentage of secondary investments qualifying for purposes of the definition of a venture capital fund. We are also excited to see the *DEAL Act* make fund-of-fund investments into VC funds qualifying. These types of investments are not currently qualifying under the SEC definition despite the prominent role of fund-of-fund investments in growing venture capital ecosystems in more regions of the country, an issue that's been supported by the SEC's Advisory Committee on Small Business Capital Formation.<sup>1</sup>

NVCA also supports *Improving Capital Allocation for Newcomers Act*, which would improve investment opportunities by increasing the permitted investor and capital limits of certain startup investments funds structured under 3(c)(1) of the Investment Company Act to 200 investors and to \$150 million, respectively. This bill would expand access to capital for emerging and smaller VC fund managers and the small companies in which they invest, particularly for those in nascent emerging ecosystems.

We are thrilled to see the committee spotlight improvements to the capital formation process and expand investment opportunities for both emerging fund managers and the next generation of American startups. Thank you for your leadership and efforts to increase new company creation, economic opportunity, and American competitiveness. We look forward to working with you on these important issues.

Sincerely,



Bobby Franklin  
President and CEO

---

<sup>1</sup> U.S. Securities and Exchange Commission Small Business Capital Formation Advisory Committee to Chair Gary Gensler, May 21, 2021. <https://www.sec.gov/spotlight/sbcfac/encouraging-small-regional-funds-043021.pdf>.



February 8th, 2023

The Honorable Patrick McHenry  
Chairman  
Committee on Financial Services  
U.S. House of Representatives  
Washington, DC 20515

The Honorable Maxine Waters  
Ranking Member  
Committee on Financial Services  
U.S. House of Representatives  
Washington, DC 20515

**Re: February 8<sup>th</sup> Subcommittee on Capital Markets Hearing Entitled “Empowering Entrepreneurs: Removing Barriers to Capital Access for Small Businesses”**

Dear Chairman McHenry and Ranking Member Waters:

The Small Business Investor Alliance (“SBIA”) submits these comments for the February 8<sup>th</sup> hearing of the Capital Markets Subcommittee regarding proposals to increase access to capital for small businesses. The SBIA welcomes the Financial Services Committee’s prioritization of economic growth and job creation initiatives for the 118<sup>th</sup> Congress.

SBIA is a national association that develops, supports, and advocates on behalf of policies that benefit investment funds that provide growth capital to small and mid-size businesses in the lower middle market, as well as the institutional investors that provide capital to these funds. Our membership consists of the advisers of traditional 3(c)(1) and 3(c)(7) private funds, small business investment companies (“SBICs”), rural business investment companies (“RBICs”), funds registered as business development companies (“BDCs”) under the Investment Company Act of 1940, and the investors that invest in these funds including banks, family offices, and fund of funds.

Over the last decade, this Committee has led efforts to enact reforms to the securities laws that promote small business capital formation and investor access to growing companies. The 2012 Jumpstart Our Business Startups (JOBS) Act was a landmark piece of legislation that President Obama rightfully called a “gamechanger.” Subsequent reforms that built upon the success of the JOBS Act originated in this Committee and were ultimately signed into law. Importantly, this work was done on a bipartisan basis and received broad support from businesses and investors alike.

Small businesses and their investor partners are facing an increasing number of threats to their ability to grow, hire new employees, and stay competitive. Reams of regulations, stubbornly high inflation, and the ability to hire qualified workers remain top concerns for small businesses. While these challenges exist for large companies, they are much more intense for small businesses and small business investors. A closely watched index of small business confidence

SBIA has appreciated the opportunity to work closely with Democrats and Republicans on this legislation, and we are eager to work with all members to advance this bill during this Congress.

2. ***Raising the threshold for the private fund adviser exemption under Section 203(m) of the Investment Advisers Act.*** In 2010, Congress replaced the longstanding private fund exemption from SEC registration requirements with a set of narrower exemption criteria. Amongst this criteria, advisers to private funds with less than \$150 million in assets under management (AUM) are exempt from full registration requirements. However, this \$150 million AUM threshold was too low when it was written in 2010 and it has never been raised nor even indexed for inflation since, notwithstanding the growth of the economy and evolution of the private capital markets since 2010. Members of this Committee have previously recognized – on a bipartisan basis – that reporting requirements can place a disproportionate burden upon smaller funds. Accordingly, we support the draft legislation under consideration at this hearing that raises the current exemption threshold to at least \$250 million in AUM and would require the SEC to update this level for inflation every five years.
3. ***Address the impact of the SEC's recently adopted investment adviser marketing rule on smaller funds.*** In 2020, the SEC adopted rules intended to ensure that marketing materials used by investment advisers and private funds provide the most accurate information possible to investors.<sup>5</sup> While well-intentioned, these rules have created compliance concerns for smaller private funds. Specifically, the performance disclosure requirements of the 2020 regulations do not properly consider advisers that use “European waterfall” arrangements, where performance and profit sharing are tied to an entire fund’s performance (i.e. not just the performance of a single investment). Because many smaller funds use the European waterfall agreements, compliance with aspects of the marketing rule are in some cases impossible because they are being asked to report numbers that do not yet exist. “FAQ’s” regarding the marketing rule released by the SEC in January 2023 left this problem uncorrected. SBIA believes that the SEC or Congress should provide some certainty for smaller funds regarding this issue. Honesty in marketing is a must, but reporting numbers that do not exist is not promoting honest disclosures.
4. ***Protect small, private businesses and BDC portfolio companies from the SEC climate and ESG proposals.*** As SBIA noted in recent comment letters, the SEC’s climate change disclosure proposal would impose *de facto* political mandates upon private businesses that are vendors to or part of a public company’s supply chain. These small private businesses – which the SEC has no authority to regulate – would be compelled to gather, standardize, and transmit information regarding Scope 3 emissions and other matters to reporting companies. The SEC failed to consider or analyze the impact such a requirement could have on these private businesses; if the SEC does not address this issue in the final climate disclosure rule then Congress must act. Small businesses are solely focused on survival and growth, without which ESG disclosures are meaningless.

<sup>5</sup> Investment Adviser Marketing (December 22, 2020)

March 28, 2023

The Honorable Erin Houchin (R-IN)  
U.S. House of Representatives  
1632 Longworth House Office Building  
Washington, DC 20515

Dear Congresswoman Houchin,

Thank you very much for your additional questions following my testimony before the Capital Market Subcommittee of the House Financial Services Committee on February 8, 2023. It was a great honor to appear before the Subcommittee to share my background and perspectives as a practicing fund manager of color investing in women founders and entrepreneurs of color – and to attest to the critical importance of the **Improving Capital Allocation for Newcomers (ICAN) Act** and other aspects of Chairman McHenry’s capital formation agenda.

I am delighted to provide the attached answers to your questions.

Please don’t hesitate to reach back out with any additional questions, or if some aspects of my answer are insufficiently clear.

Thank you for your service to our nation at such a critical time in its history, and for your support for legislation that will help get more capital to women founders and entrepreneurs of color.

Respectfully,

McKeever “Mac” Conwell II  
Founder and Managing Partner  
RareBreed Ventures  
Baltimore, MD

**Empowering Entrepreneurs: Removing Barriers to Capital Access for Small Businesses**  
02/08/2023 @ 2 PM

**Rep. Houchin questions for Mac Conwell:**

1. Startups and entrepreneurs often face difficulties in raising capital. Thankfully, the JOBS Act of 2012 addressed some of these challenges, including Title II, which made it easier for startups to market their securities through general solicitation or advertising. Can you share how the JOBS Act's Rule 506(c) reforms helped you when you started your first fund?

When I decided to raise RareBreed Ventures Fund I, I had already been a successful entrepreneur and had spent 4 years working as an early-stage venture investor for the state of Maryland. I knew startups, I understood investing and evaluating in startups, but I didn't have a network of wealthy people and institutions to raise the fund from.

It was thanks to the JOBS Act's Rule 506(c) that I was able to use social media, Twitter mainly, to meet with many potential investors. By sharing my knowledge of the industry with the public and democratizing information about venture capital with Twitter I was able to grow a community of other investors and founders. This allowed me to have 1,128 meetings in my first 90 days of fundraising. Eventually, I would have more than 4,000 meetings over 18 months to fully raise RareBreed Fund I. The vast majority of these meetings came from accredited investors I met on Twitter, heard me on podcasts, or read some of my long-form material.

The ability to publicly solicit my fundraising thanks to the JOBS Act's Rule 506(c), allowed me to use the platforms at my disposal to share my abilities and qualification. That then gave me the opportunity to meet with investors who otherwise would not have ever heard of or met with me. If not for the JOBS Act's Rule 506(c) RareBreed Ventures would probably not exist today and the 17 companies I was the first investor in since 2021, may not exist today as well.

2. Early-stage companies typically rely on exemptions from Securities Act registration requirements to raise capital while avoiding the high costs of going public. Many of these exemptions require their investors to be Accredited Investors. As an entrepreneur without an existing network of Accredited Investors, you mentioned having to find qualified investors in your first fund on Twitter. With that experience in mind, can you compare the challenges you faced versus the challenges of fund managers graduating from Ivy League schools or based in traditional VC hubs?
  - a. Would any of the policies discussed at the hearing make it easier for entrepreneurs like yourself to raise capital?

The Improving Capital Allocation for Newcomers (ICAN) Act which increases the number of investors in a fund would make it easier for fund managers like

**Empowering Entrepreneurs: Removing Barriers to Capital Access for Small Businesses**

02/08/2023 @ 2 PM

myself to raise capital. By increasing the number of investors in a fund, you effectively reduce the minimum size of the investment in a fund, which in turn increases the size of the pool of investors who have the ability to make an investment into a fund. By increasing the pool of investors who can make investments into a fund, you are also increasing the amount of capital available to the asset class. More investors and capital to the asset class means more new fund managers like myself from a wider range of backgrounds and investing in a wider range of founders and geographies.

- b. How would easier access to capital help entrepreneurs and their communities outside the traditional VC hubs?

Easier access to capital means more capital being managed by more fund managers. This leads to greater diversity in investment approaches beyond what we see in the traditional VC hubs. For example, take the woman I mentioned in my testimony, Shawna Stepp-Jones. She is a Black woman from Baltimore building a product to help hair stylists with a focus on Black women. Well, thanks to the amendment to the Investment Company Act of 1940 which allowed me, a Black man from Baltimore to raise from up to 250 limited partners. I was able to start RareBreed Ventures and in turn, make an investment in Shawna's business after no one else would because they didn't understand her or her community. Today Shawna has a thriving business that employs other women from Baltimore and is inspiring young women. That amendment to the Investment Company Act of 1940 made it easier for me to raise my fund, which allowed me to offer a different investment approach that led me to make investments in founders like Shawna. Giving her an easier pathway to capital and allowing her to be in a position to empower her community where many have felt overlooked or uncared for.

3. The SEC's Small Business Advocate reported last December that there has been a steady rise in the number and amount of crowdfunding offerings, supporting more diverse founders and more geographically diverse companies across the country. In fact, 70 percent of capital raised under Reg CF is distributed outside the top 10 traditional capital hubs. Why is equity crowdfunding a crucial tool for startups and founders when it comes to raising capital?

The fact that 70 percent of capital raised under Reg CF is distributed outside the top 10 traditional capital hubs says it all. Before Reg CF startup founders were beholden to

**Empowering Entrepreneurs: Removing Barriers to Capital Access for Small Businesses**  
02/08/2023 @ 2 PM

investors concentrated in the top 3 traditional capital hubs. This meant to get noticed and funded a founder had to have a network of investors in those markets, move to those markets, or struggle to ever get off the ground because they didn't even know those were the places where investors were. This is to say that the vast majority of American entrepreneurs were either forced to move from their communities or struggle in those communities with limited resources.

What Reg CF has already shown us is that amazing companies and products that people want to support and invest in are everywhere. It also shows us that non-accredited retail investors want to support founders from their communities while also participating in the upside of the business they are building. If not for Reg CF many founders, especially those from underrepresented communities, would be beholden to traditional VC hubs that had repeatedly ignored the majority of American founders because of their location, sex, race, or lack of exposure. Reg CF is truly important because it levels the playing field for all Americans raising capital for their company no matter who they are or where they live. To me, Reg CF is the north star of the American dream for all and not just the privileged few.

4. You are aware that Section 3(c)(1) of the Investment Company Act of 1940 exempts funds with fewer than 100 beneficial owners (all of whom must be accredited investors) from registration as an investment company. It also includes an exemption for qualified venture funds with fewer than 250 beneficial owners and \$10 million in aggregate capital contributions and uncalled capital commitments. Can you explain, based on your experience, the difficulties in complying with these thresholds?

In my mind, there are two major difficulties in complying with these thresholds and they go hand and hand. The first is the limit on beneficial owners or limited partners effectively limits the minimum investment that can be made into a fund. For example, if you are raising a \$75 million dollar fund and are limited to 100 beneficial owners, then the minimum someone can invest into that fund would be \$750 thousand dollars. There are only so many people who could make a \$750 thousand dollar investment, let alone a \$750 thousand dollar investment that is illiquid for ten years. This keeps a wide portion of accredited investors from participating in the asset class.

That is the second issue here. These thresholds create an environment where many accredited investors can't participate which severely limits the network of organizations and individuals who could participate. Meaning you need to have connections to or be a part of these limited networks of organizations and individuals which often aren't very diverse. This is a particularly painful issue for me and my fund RareBreed Ventures because our first fund has 194 limited partners thanks to the amendment to Section

**Empowering Entrepreneurs: Removing Barriers to Capital Access for Small Businesses**

02/08/2023 @ 2 PM

3(c)(1) of the Investment Company Act of 1940 which allows for 250 beneficial owners in a fund of \$10 million or less. Unfortunately, 162 out of 194 of our beneficial owners, 83%, made investments of \$50 thousand or less. With RareBreed Ventures fund two planning to be more than \$10 million almost none of those 162 accredited investors will be able to continue to invest in RareBreed Ventures going forward. Many of these limited partners in RareBreed Ventures fund one are members of my community, first-time investors in a fund, or individuals who believe in our mission.

Thanks to these thresholds I'll no longer be able to seek investment capital from these current investors no matter how happy they are with my work or how badly they want to invest. Now I am forced to raise my second fund from organizations and individuals who may not care about my community or RareBreeds mission or look like me or have experience working with a fund manager like me. This only makes it that much more difficult to raise a fund and make investments in innovation to drive our great nation forward. These limits on the types and amounts of capital a fund manager can raise through these thresholds only serves to limit innovation, job creation, and economic growth.

**Rep. Lawler questions for Deborah Gladney**

1. Small businesses make up 99 percent of all enterprises in the U.S. and employ almost half of the workforce, yet in 2020, 80 percent of small businesses reported financial difficulty. As a founder of a small business, what challenges did you face when starting your business?

Most people have likely considered starting a business at some point. However, most choose not to because of the lack of knowledge or resources for starting. This was the same barrier we had.

- a. How would your company have benefitted from policies that made it easier to raise capital?
    - i. We would spend less time raising/trying to figure out how to raise and more time building a company. A company that's based in a community that needs innovative companies like ours.
  - b. Would policies that reduce fundraising costs make it easier or harder to hire and retain skilled employees?
    - i. It's impossible to hire without capital. And it's impossible to start most companies without capital. Having policies that puts capital in founders' hands faster has a direct impact on being able to hire faster, and thus, retain faster.
  - c. What impact would that have on your community?
    - i. According to the Chung Report, our community attracted \$5.4 million in venture capital investment in the past two years. Peer cities Omaha and Des Moines attracted \$20.8 million and \$130 million, respectively. Our community is severely underfunded. Removing barriers would bring more opportunity to this area that is vastly underserved.
2. Data shows that nearly 30 percent of founders who received VC funding in 2019 had Ivy League degrees. Although there has been a record high of total VC investments in recent years, only three percent of venture dollars went to women, black and Latino founders. As you and your sister were the first black women in your state to secure more than \$1 million in venture funding, can you talk about the challenges you faced while searching for potential investors?

This is a great observation because, oftentimes, the few women/minority founders who DO get funded usually have ivy league degrees. It gives investors a false sense of comfort to invest in a minority if they have an ivy league degree.

- a. Can you explain the impact that venture funding had on your company and how it enabled your company to grow?
  - i. Our company, WorkTorch, now has 10 employees, serves over 80,000 job seekers, and more than 50 employers in 30 states. None of this would be possible had we not obtained venture funding.
- b. How did this growth impact your community?

**Empowering Entrepreneurs: Removing Barriers to Capital Access for Small Businesses**  
02/08/2023 @ 2 PM

- i. All of the growth mentioned above is primarily taking place in our community - Wichita, Kansas.

3. Does the success of your company in securing venture funding and growing your business give aspiring entrepreneurs from your community the confidence to start their own businesses?

Absolutely. We have so many "strikes" against us. We're black. We're women. We're in Kansas. We're parents. We're non-ivy league. We're non technical. The list goes on. If we can do it, then anyone can. With the RIGHT support.

- a. In light of this, should Congress pursue policies that make it easier for entrepreneurs throughout the country to secure venture funding and not just in Silicon Valley and Boston?
  - i. Yes. Talent is equally distributed across the United States, but opportunity is not. 75% of all venture capital investments go to just three metro areas with Silicon Valley being at the top of the list.
- b. Will any of the policies discussed at the hearing help achieve this objective?
  - i. All of them will help accomplish this in a different way.

4. How much more challenging is it for small businesses to find potential investors when they are located in places that lack established, robust capital raising networks?

This is a relationship-based industry. So if you live in a community without an established network, you have no network.

- a. In these ecosystems, "finders" may play a crucial role in providing access to capital for smaller businesses. However, companies that want to follow the rules struggle to determine when they can engage "finders" who are not registered as broker-dealers. If we clarify this by exempting "finders" from registration, would "finders" become a useful tool for connecting small businesses with investors outside of established tech and VC hubs?
  - i. Absolutely. We were only able to obtain venture funding because of an introduction. And this is the case for almost every venture-backed company. It's extremely difficult to infiltrate without someone connecting you to the network.



Center for American  
Entrepreneurship

February 8, 2023

The Honorable Patrick McHenry (R-NC)  
Chairman  
House Financial Services Committee  
2129 Rayburn House Office Building  
Washington, DC 20515

The Honorable Maxine Waters (D-CA)  
Ranking Member  
House Financial Services Committee  
2129 Rayburn House Office Building  
Washington, DC 20510

The Honorable Ann Wagner (R-MO)  
Chair  
Subcommittee on Capital Markets  
2129 Rayburn House Office Building  
Washington, DC 20515

The Honorable Brad Herman (D-CA)  
Ranking Member  
Subcommittee on Capital Markets  
2129 Rayburn House Office Building  
Washington, DC 20510

Dear Chairmen McHenry and Wagner and Ranking Members Waters and Sherman,

On behalf of the [Center for American Entrepreneurship](#) (CAE) and the millions of American entrepreneurs who work every day to launch and build the new businesses that drive economic growth, job creation, and opportunity, I write today to thank you for conducting today's hearing "Empowering Entrepreneurs: Removing Barriers to Capital Access for Small Businesses."

Starting a new business requires money. In the initial days of a startup, capital needs may be limited to the bare essentials – money to purchase supplies, computers, and other office equipment. But as new businesses begin to grow, capital needs multiply. Entrepreneurs need money to pay bills, move out of the garage or dining room into office space, and, hopefully, begin paying initial employees. Most importantly, entrepreneurs need capital to further develop their product or service idea, research the marketplace, and develop and implement a strategy for identifying and targeting customers. Because such costs typically arrive long before the first dollar of revenue, capital and credit are the lifeblood of any new business.

The Jumpstart Our Business Startups ("JOBS") Act of 2012 – for which Chairman McHenry was a principal drafter and sponsor – was the most significant capital formation legislation in many years, improving new and small business access to capital by easing burdensome securities regulations and legalizing crowdfunding. Ten years later, it's clear there is more work to do. At roundtables that CAE regularly conducts with entrepreneurs across the country, difficulties in securing the capital they need is a top issue raised by participants.

Current capital access difficulties not only include regulatory and procedural barriers, but also wide and persistent disparities along gender, racial, and geographic lines. While white male entrepreneurs in coastal cities generally enjoy favorable access to multiple sources of capital, women founders, entrepreneurs of color, and new and small business owners in heartland states and rural communities encounter significant barriers to securing the capital they need to thrive.

The capital formation agenda to be discussed at today's hearing – including the Improving Crowdfunding Opportunities Act, the Small Entrepreneurs Empowerment and Development (SEED) Act, the Developing and Empowering our Aspiring Leaders (DEAL) Act, the Improving Capital Allocation for Newcomers (ICAN) Act, the Regulation A+ Improvement Act, the Unlocking Capital for Small Businesses Act, and the Helping Angels Lead our Startups (HALOS) Act – would significantly improve capital access for new and small businesses on multiple fronts.

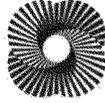
In particular, the ICAN Act would dramatically improve the gender, racial, and geographic distribution of capital. By raising the cap on exempt investment funds organized under section 3(c)(1) of the Investment Company Act of 1940 and raising the number of permitted accredited investors, the average investment required to participate in funds would be reduced, allowing more women and people of color to participate in funds investing in women founders and entrepreneurs of color. Research has demonstrated that who gets funded depends a great deal on who is doing the investing – a phenomenon known as “homophily.” Investors tend to invest in entrepreneurs who look like them, have similar life experiences, and who are launching companies the investors understand and can relate to. A more diverse investor base, therefore, is critical to ensuring greater diversity among entrepreneurs who receive capital.

It is important to emphasize that the ICAN Act would also significantly enhance investor protection. First, only accredited investors may participate in such funds. Second, raising the number of permitted investors will divide investment funds by a larger number, reducing the average exposures of participating investors. With reduced exposures to particular funds, investors would be free to allocate their limited capital across multiple funds, diversifying their portfolios and reducing their investment risk.

CAE thanks the membership of the House Financial Services Committee and each of you for your leadership regarding these critical capital formation issues. We look forward to working with you to enact the Committee's capital formation agenda.

Sincerely,

John R. Dearie  
President  
Center for American Entrepreneurship



U.S. Chamber of Commerce

1615 H Street, NW  
Washington, DC 20062-2000  
uschamber.com

February 8, 2023

The Honorable Patrick McHenry  
Chair  
Committee on Financial Services  
Services  
U.S. House of Representatives  
Representatives  
Washington, DC 20515

The Honorable Maxine Waters  
Ranking Member  
Committee on Financial  
U.S. House of  
Washington, DC 20515

Dear Chair McHenry and Ranking Member Waters:

The U.S. Chamber of Commerce appreciates the Capital Markets' Subcommittee for holding the hearing "Empowering Entrepreneurs: Removing Barriers to Capital Access for Small Businesses." In 2012, a divided Congress came together to pass the Jumpstart Our Business Startups (JOBS) Act, landmark legislation that reduced the bureaucratic barriers to raising capital and helped spur business growth and innovation on an economywide scale. The 118th Congress has an opportunity to build off that success, and this hearing is a critical first step.

We look forward to engaging with the Committee in advancing this goal and support the following legislation.

**Support**

**H.R. The Improving Crowdfunding Opportunities Act**

The "Improving Crowdfunding Opportunities Act" would add continuity to the regulation of secondary transactions involving crowdfunding vehicles and clarify legal liability for crowdfunding portals.

**H.R. The Small Entrepreneurs' Empowerment and Development (SEED) Act**

The "Small Entrepreneurs' Empowerment and Development (Seed) Act" would provide an exemption from state and federal registration requirements for "micro" offerings that do not exceed \$250,000 in the aggregate. This would benefit entrepreneurs who are looking to raise relatively small amounts of capital and cannot afford costly legal and registration requirements. Importantly, this bill would also prevent bad actors from participating in such offerings.

**H.R. to direct the SEC to update its definition of "small entities" under the Regulatory Flexibility Act**

Small and startup businesses often bear a disproportionate cost of regulation, and the Chamber has long held concerns that many SEC rules are not properly calibrated in a way that balances investor protection with the SEC's mandate to facilitate capital formation. This bill would direct the SEC to modernize the criteria it uses to define a "small entity" to reflect the growth of the U.S. economy and the evolution of the capital markets since the last time the small entity definition was addressed. The Chamber believes that requiring the SEC to issue a report every five years on the definition of "small entity" is duplicative.

**H.R. The Developing and Empowering our Aspiring Leaders Act of 2023**

The "Developing and Empowering our Aspiring Leaders Act" would impact Registered Investment Adviser (RIA) rules promulgated by the SEC that have disincentivized some venture capital funds from investing in Emerging Growth Companies (EGCs). The 2010 Dodd-Frank Act sought to exempt venture capital funds from the costs and challenges associated with becoming an RIA. However, the definition of "venture capital fund" promulgated by the SEC pursuant to Dodd-Frank was too narrow and did not meet the Dodd-Frank statutory obligations of a full venture capital exemption. The current definition ignores critical elements and developments related to the venture capital industry, including growth equity firms which can often be investors in EGCs around the time they are considering a public offering. Shares of EGCs, including the purchase of EGC shares on the secondary market, should be considered qualifying investments. Creating a more accurate venture capital exemption definition – which the DEAL Act would do – would expand the pool of possible investors for EGCs.

**H.R. The Improving Capital Allocation for Newcomers Act of 2023**

This bill would promote venture capital investing in all regions of the country. The bill would make changes to the requirements for a fund to be able to rely on the qualifying venture capital fund exemption under Section 3(c)(1) of the Investment Company Act. This legislation would help mitigate regulatory burdens that can disincentivize fund formation and choke off capital to startup firms. The Chamber has previously noted the need for the United States to maintain its global edge in venture capital and early stage investing due to increased competition from China.

**H.R. The Regulation A+ Improvement Act of 2023**

The "Regulation A+ Improvement Act" would make a public offering more economically feasible for companies that are not prepared to undertake a full initial public offering (IPO) by increasing the permissible amount for a public offering up to

\$150 million. Similar to the Title III crowdfunding provisions, Title IV of the JOBS Act – which was intended to revitalize the “Reg A” offering market – can still be galvanized, due in part to the fact that compliance costs have continued to increase for smaller firms, but companies remain limited to the amount of capital they can raise under Reg A.

**H.R. The “Helping Angels Lead Our Startups Act”**

The “Helping Angels Lead Our Startups Act” would help startup businesses attract investors by clarifying the definition of “general solicitation” under Title II of the JOBS Act. When finalizing rules under Title II of the JOBS Act, the SEC regrettably put in place provisions that would effectively bar certain types of communication between startups and angel investors, who are a critical source of capital in the economy. The Act would simply clarify that startups and angel investors are permitted to participate in “demo days” or other events in which no specific investment solicitation is made. This is consistent with the original intent of the JOBS Act and would help innovative companies expand and hire new employees.

**H.R. to amend the Investment Advisers Act of 1940 to increase the exemption from registration thresholds for certain investment advisers of private funds**

This bill would increase the assets under management (AUM) threshold for funds that can rely on the “private fund exemption” for SEC registration from \$150 million to \$250 million. When Congress enacted the \$150 million threshold in 2010, it did not index that number to inflation. Congress has not revisited the threshold, even though the economy has grown substantially and private markets have evolved since 2010. Increasing the threshold to \$250 million – and requiring the SEC to index that number for inflation every five years – would help mitigate regulatory burdens for small private funds and enhance their ability to deploy capital to small and middle market businesses throughout the country.

Thank you for the opportunity to express our views.

Sincerely,

A handwritten signature in black ink, appearing to be 'TK' followed by a long horizontal flourish.

Tom Quadman  
Executive Vice President  
Center for Capital Markets Competitiveness  
U.S. Chamber of Commerce

cc: Members of the House Committee on Financial Services

2/14/23, 3:20 PM

An Iowa Farmer Tried to Dodge Stock-Market Turmoil. It Cost Him \$900,000. - WSJ

This copy is for your personal, non-commercial use only. Distribution and use of this material are governed by our Subscriber Agreement and by copyright law. For non-personal use or to order multiple copies, please contact Dow Jones Reprints at 1-800-843-0008 or visit [www.djreprints.com](http://www.djreprints.com).

<https://www.wsj.com/articles/regulation-d-private-offering-debt-equity-11673625595>

MARKETS THE INTELLIGENT INVESTOR

## An Iowa Farmer Tried to Dodge Stock-Market Turmoil. It Cost Him \$900,000.

Brokers and financial advisers are steering clients to assets that don't trade. Such securities can often be dodgy, sometimes lose all their value—and getting out is a lot harder than getting in.



ILLUSTRATION: ALEX NABAUM



By Jason Zweig [Follow](#)

Jan. 13, 2023 11:02am ET

Over the past two years, bonds have lost almost 15% and stocks have barely gained 5%, whipsawing investors along the way. That's what markets do.

As a result, financial firms are pile-driving their clients into assets that have no market. Over the past two years, investors bought an astonishing \$878.9 billion in so-called Regulation D private offerings of debt and equity that don't trade, according to SLCG Economic Consulting, a research firm in McLean, Va.

These are different from Reg D offerings of "pooled investment funds," which can include private-equity, venture-capital and hedge funds from major firms. Many of these other corporate offerings instead come directly from tiny issuers or through dodgy brokers and financial advisers.

<https://www.wsj.com/articles/regulation-d-private-offering-debt-equity-11673625595>

1/4E

2/14/23, 3:20 PM

An Iowa Farmer Tried to Dodge Stock-Market Turmoil. It Cost Him \$900,000. - WSJ

### Number of Regulation D corporate offerings



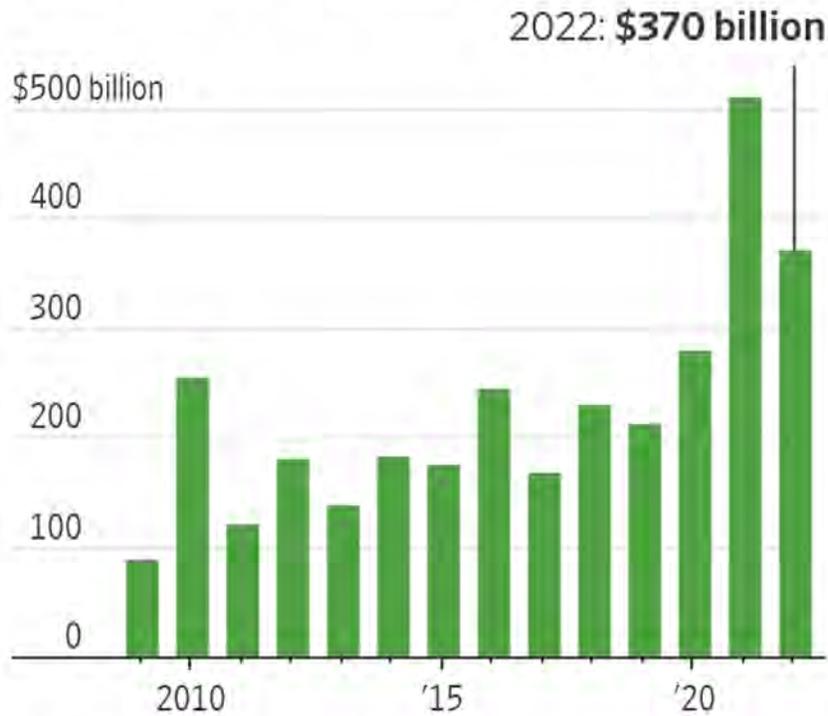
<https://www.wsj.com/articles/regulation-d-private-offering-debt-equity-11673625595>

2/E

2/14/23, 3:20 PM

An Iowa Farmer Tried to Dodge Stock-Market Turmoil. It Cost Him \$900,000. - WSJ

## Amount of securities sold



Note: Does not include pooled investment funds

Source: SLCG Economic Consulting analysis of Securities and Exchange Commission filings

And, to be blunt, they are often dreck. The investments sometimes end up worthless, and egregious conflicts of interest are rife among those selling them.

2/14/23, 3:20 PM

An Iowa Farmer Tried to Dodge Stock-Market Turmoil. It Cost Him \$900,000. - WSJ

The pitch for the private corporate offerings: Your bonds, which were supposed to be ballast for your stocks, have turned into torpedoes, and your stocks could get blown away any day.

Private placements of debt, equity and other assets don't move in sync with public markets—and, because they don't trade, their reported prices fluctuate much less.

They offer the hope of higher returns, since these smaller issuers often have to pay more to obtain capital. And, hey, every corporate titan started out tiny, and many legitimate companies have offered securities in this private market.

The fatal flaw: You can't always sell when you want to, and often you can't sell at all. Financial disclosures range from minimal at best—an offering document, perhaps cursory annual or quarterly reports—to nonexistent. The risk of default or bankruptcy is high. Commissions and other fees can easily exceed 10%.

I can hear professional investors muttering right now with a smirk: Look at the dumb money, rushing to buy these black boxes that don't trade, charge high fees, offer limited information and can often turn out to be fraudulent.

Coming from people who've poured trillions into hedge funds and other bundles of opacity, that criticism is a crock.

The individual investors buying these unregulated private offerings aren't stupid. They believe they're buying safe and potentially lucrative assets from someone they trust.

"The power and prowess of a good sales pitch will win the day every day," says Andrea Seidt, securities commissioner for the state of Ohio. Unfortunately, she adds, "bad actors flock to these dark spots in the market, because of the opportunity to take advantage of investors."

This week I spoke to a half-dozen individuals who bought into the promise of private placements and got frozen—or wiped out.

Jeff Temeyer, 64 years old, is a semiretired farmer in Independence, Iowa. In 2016 he invested in private debt and equity in a Texas cancer-treatment facility offered by a local broker, Dana Vietor. Mr. Temeyer, who says he was told he would earn at least 8% annually, invested more than \$900,000 in all—only to learn that the securities were near-worthless.

In 2020, Mr. Vietor was barred for life by the Financial Industry Regulatory Authority, which oversees how brokers do business. In November 2022, Finra arbitrators ordered Mr. Vietor to

pay Mr. Temeyer and 10 other investors a total of \$5.7 million in damages and other compensation. Mr. Vietor's lawyer didn't return requests for comment.

Jill Jester, 79, of Muncie, Ind., inherited a basket of private offerings in her husband's individual retirement account after he died in 2020.

They, too, have turned out to be worthless, says her attorney, Bruce Oakes of Oakes & Foshier LLC in St. Louis. In October 2022, a Finra arbitration panel awarded Ms. Jester more than \$420,000 in damages and other compensation from her former broker's firm.

It's disconcertingly common for the smaller of these private deals to be riddled with conflicts of interest.

Executives at the brokerages or financial-advisory firms selling these offerings may also serve as officials of the companies they are raising money for.

Mr. Vietor, for example, also was an owner and manager of the cancer facility he got his clients to invest in—even though he lacked extensive experience as a healthcare manager and often didn't fully disclose his interest to clients, according to investors and their lawyers.

Because Regulation D companies aren't obligated to issue current financial statements, investors can remain in the dark even as they sink deeper and deeper into the hole.

Mr. Temeyer's attorney, Gail Boliver of Marshalltown, Iowa, says Mr. Vietor kept selling securities even after the cancer facility foundered: "It was like selling tickets on the Titanic after it hit the iceberg."

I also spoke this week with an investor whose broker invested approximately 70% of her 401(k) in debt securities issued under Regulation D.

Only after it was too late did she realize that was like getting almost three-quarters of her retirement assets encased in quick-drying concrete. She can't get her money out, and the value of what's left is uncertain.

"I would like to sell," she says, "but there's no market."

In fact, it's often illegal to sell these private offerings to anyone else, unless the broker or financial adviser who sold them to you takes them off your hands.

2/14/23, 3:20 PM

An Iowa Farmer Tried to Dodge Stock-Market Turmoil. It Cost Him \$900,000. - WSJ

Investors can avoid such headaches by trusting—but verifying. Buy nothing whose fees aren't explicitly disclosed upfront in writing. Buy nothing without a prospectus or offering memorandum that discloses financial data, risks and conflicts of interest. Be wary of anybody who suggests putting private placements in your IRA or 401(k).

Alternative investments—anything but publicly traded stocks, bonds and real estate—have been all the rage in recent years. And you might well want an alternative to losing money. Just make sure you don't end up with an alternative to making it instead.

Write to Jason Zweig at [intelligentinvestor@wsj.com](mailto:intelligentinvestor@wsj.com)

*Appeared in the January 14, 2023, print edition as 'An Iowa Farmer's \$900,000 Investing Mistake'.*



**NASAA REPORT AND  
RECOMMENDATIONS  
FOR REINVIGORATING  
OUR CAPITAL MARKETS**

Published February 7, 2023



## About NASAA

Organized in 1919, the North American Securities Administrators Association (“NASAA”) is the oldest international organization devoted to investor protection. NASAA is a voluntary association whose membership consists of the securities regulators in the 50 states, the District of Columbia, Puerto Rico, and the U.S. Virgin Islands (collectively referred to below as “state securities regulators”), as well as the 13 provincial and territorial securities regulators in Canada and the securities regulator in México. In the United States, NASAA is the voice of state securities regulators that protect investors, promote responsible capital formation, and support inclusion and innovation in the capital markets. NASAA members license firms and their agents, investigate alleged violations of securities laws, file enforcement actions when appropriate, and educate the public about investment fraud. NASAA members also participate in multi-state enforcement actions and information sharing. For more, visit: <https://www.nasaa.org/>.

Follow and Subscribe

[LinkedIn](#) | [Twitter](#) | [YouTube](#) | [NASAA Talks Podcast](#) | [NASAA.org Updates](#)

## Table of Contents

<b>About NASAA</b> .....	2
<b>Introduction</b> .....	4
<b>I. Strengthening Public Markets</b> .....	5
A. Public Disclosure Is Valuable.....	6
B. Private Offerings Under Rule 506 Are Now Dominant .....	7
C. The 2012 JOBS Act Did Not Achieve Its Goals for the Public Markets.....	11
D. The Current Incentives to Go Public Are Minimal .....	16
<b>II. Helping Small Businesses and Entrepreneurs</b> .....	18
A. Regulation A and Regulation Crowdfunding Cannot Compete with Regulation D.....	19
B. Companies Need a Stronger Public Market, Not More Ways to Stay Private .....	21
C. Preemption Harms Small Business Capital Formation.....	22
<b>III. Increasing Opportunities for Investors</b> .....	24
A. Investors Are Well-Served by the Public Markets .....	24
B. Investors Are Not Missing Out on Private Market Opportunities .....	25
1. <i>The Inherent Disadvantages to Retail Investors in Private Offerings</i> .....	25
2. <i>The Lack of Retail Investor Demand for Private Offerings</i> .....	27
<b>IV. NASAA’s Agenda for Reinvigorating the Capital Markets</b> .....	30
A. Promoting Responsible Capital Formation .....	30
B. Protecting Investors of All Ages and Backgrounds .....	31
C. Supporting Inclusion and Innovation in Our Capital Markets.....	33
<b>Appendix</b> .....	35

## Introduction

State securities regulators play several vital roles in our capital markets. In addition to serving on the front lines of protecting Main Street investors, we are on the front lines of helping Main Street businesses understand their capital-raising options. Our work to promote responsible capital formation translates into job creation and other economic support for local communities throughout our states.

Released in April 2022, the draft Jumpstart Our Business Startups Act of 2022 (the “JOBS Act 4.0”) is made up of various legislative proposals intended to build upon the original Jumpstart Our Business Startups Act that was enacted in 2012 (the “2012 JOBS Act”).<sup>1</sup> As explained in this report and the Appendix hereto, we are concerned that a majority of the proposals in the JOBS Act 4.0 would erode our public markets further and adversely affect the businesses and investors that rely on those markets to raise investment capital and build sound financial futures. Moreover, the ideas would move us further away from important foundational principles in our system of securities regulation and undermine the longstanding efforts of state securities regulators to strengthen our public markets, support a healthy ecosystem for entrepreneurs and small businesses to raise capital successfully, and increase opportunities for investors.

As detailed in Part IV below, we urge Congress to oppose the JOBS Act 4.0 as published in April 2022 and as modified during the 118th Congress.<sup>2</sup> Relatedly, we urge Congress to join NASAA

<sup>1</sup> [2012 JOBS Act](#), Pub. L. No. 112-106, 126 Stat. 306 (2012). Following the 2012 JOBS Act, Congress passed the Fixing America’s Surface Transportation Act (the “FAST Act”), Pub. L. No. 114-94 (2015), which was unofficially dubbed “JOBS Act 2.0.” On July 17, 2018, the U.S. House of Representatives passed the “JOBS and Investor Confidence Act of 2018,” Pub. L. No. 114-94, S.488, 115<sup>th</sup> Congress (2017-2018); it was a compilation of 32 bills and was considered “JOBS Act 3.0.” See Glenn Pollner, Elizabeth Ising & Thurston Hamlette, [JOBS Act 3.0](#), Harvard Law School Forum on Corporate Governance (Aug. 6, 2018).

<sup>2</sup> The House Financial Services Committee (“HFSC”), Subcommittee on Capital Markets has noticed related bills, all marked discussion draft, in connection with two hearings that it will hold on February 8, 2023. Some of them were included in the JOBS Act 4.0 published in April 2022—specifically, (1) the [Gig Worker Equity Compensation Act](#); (2) the [Increasing Investor Opportunities Act](#); (3) the [Equal Opportunity for All Investors Act of 2023](#); (4) the [Improving Crowdfunding Opportunities Act](#); (5) the [Small Entrepreneurs Empowerment and Development Act of 2023](#); (6) the [Developing and Empowering Our Aspiring Leaders Act of 2023](#); (7) the [Unlocking Capital for Small Businesses Act of 2023](#); and (8) to [direct the SEC to update its definitions of “small entities”](#). NASAA’s position on each of them is set forth in the Appendix hereto. The following bills were not included in the April 2022 JOBS Act 4.0: (1) the [Fair Investment Opportunities for Professional Experts Act](#); (2) the [Accredited Investor Definition Review Act](#); (3) the [Accredited Investor Self-Certification Act](#); (4) the [Investment Opportunity Expansion Act](#); (5) to [expand the definition of “accredited investor”](#); (6) to [preempt blue sky laws for off-exchange secondary trading](#); (7) the [Improving Capital Allocation for Newcomers Act of 2023](#); (8) the [Regulation A+ Improvement Act of 2023](#); (9) to [amend the Investment Advisers Act of 1940 to increase the exemption from registration threshold](#); and (10) the [Helping Angels Lead Our Startup Act of 2023](#). As explained in the Appendix hereto with respect to the Equal Opportunity for All Investors Act, NASAA has serious concerns with proposals to expand the universe of persons who qualify as an accredited investor. Congress should direct the SEC to study, in consultation with NASAA, the anticipated consequences for the U.S. capital markets of legislation to expand the universe of accredited investors. Further, NASAA strongly opposes the proposal to preempt state blue sky laws for off-exchange secondary trading

and state securities regulators in prioritizing proposals that will reinvigorate our capital markets. For example, stronger regulatory coordination is critical to the preservation of our capital markets. Accordingly, we support the Promoting Opportunities for Non-Traditional Capital Formation Act,<sup>3</sup> which would expand the functions of the Office of the Advocate for Small Business Capital Formation at the U.S. Securities and Exchange Commission (“SEC,” “Commission” or “agency” as appropriate) and require meetings with state securities regulators at least annually.<sup>4</sup>

In addition to better coordination, better data, especially on the private markets, is desperately needed. Regulators have almost no visibility into private offerings, and for years, we have urged the SEC to amend its rules so it can collect critical data about these offerings to support evidence-based rulemaking.<sup>5</sup> Congress should require the SEC to make these changes and, further, should direct the SEC to conduct a holistic study of the capital markets and how best to restore the primacy of the public markets. This study, we believe, would illustrate the need for bolder action, including passage of the Private Markets Transparency and Accountability Act,<sup>6</sup> which would restore balance between public and private markets by requiring large companies to start filing public reports.

### I. Strengthening Public Markets

From its inception in the 1930s, federal securities regulation has been built upon a philosophy of disclosure. This philosophy involves a fundamental bargain: if a company wishes to sell its securities to the general public, then it must disclose detailed information about the business publicly.<sup>7</sup> Under this approach, all material facts and associated risks of an investment are fully disclosed to prospective investors so they can make informed investment decisions. Access to this information empowers investors to educate and defend themselves.

---

for the same reasons we oppose similar legislation such as the [Facilitating Main Street Offerings Act](#), which was introduced during the 117<sup>th</sup> Congress and included in the April 2022 JOBS Act 4.0.

<sup>3</sup> H.R. 7977, [Promoting Opportunities for Non-Traditional Capital Formation Act](#), 117<sup>th</sup> Congress, 2<sup>nd</sup> Session. See also [NASAA Letter to Congress Re: H.R. 7977](#) (June 10, 2022).

<sup>4</sup> Section 19(d) of the Securities Act of 1933 (“Securities Act”), 15 U.S.C. § 77s, provides that the Commission is authorized to cooperate and share information with NASAA, and the Commission is required to conduct an annual conference to facilitate such cooperation. The Promoting Opportunities for Non-Traditional Capital Formation Act would enhance the existing coordination by facilitating more direct communication between NASAA and the SEC’s Office of the Advocate for Small Business Capital Formation.

<sup>5</sup> See [NASAA Letter to Congress](#) Regarding the JOBS Act 2.0 (May 6, 2014).

<sup>6</sup> S. 4857, [Private Markets Transparency and Accountability Act](#), 117<sup>th</sup> Congress, 2<sup>nd</sup> Session.

<sup>7</sup> See Usha Rodrigues, [Financial Contracting with the Crowd](#), 69 EMORY L.J. 397 (2019) at II.A (“For years, an equilibrium of sorts existed in the securities world, one rooted in a strict divide between two markets. On one side of the divide lay private markets, policed by fraud, which allowed for relatively small-scale fundraising from wealthy individuals and institutions. Resale of securities was both legally and practically difficult. On the other side lay public markets, policed by disclosure, which allowed companies to raise millions of dollars and enjoy a liquid secondary market.”)

More specifically, a public reporting company must register with the SEC by filing a Form 10 that describes its business in detail, including its financial condition, and thereafter must make periodic filings (e.g., Forms 10-K, 10-Q, and 8-K) to disclose ongoing developments related to its finances and business environment. A public reporting company also must comply with proxy regulations that give shareholders the ability to cast informed votes on important matters related to the governance of the company, including executive compensation and the election of board members. Once registered, the company can make an initial public offering (“IPO”) of its securities and, if the company chooses to list its securities on a national securities exchange, it must meet minimum quantitative and qualitative listing standards, including requirements related to independent directors, conflicts of interest, and shareholder approval of certain corporate actions.

#### A. Public Disclosure Is Valuable

The disclosure requirements in the United States provide important protections for investors and serve as the foundation for a vibrant marketplace that is often described as the envy of the world.<sup>8</sup> Our public equity markets are the deepest and most liquid, and they provide efficient engines for companies to raise trillions of dollars in capital. While our markets are not flawless, and we believe certain market structure reforms would be helpful, it is important to remember that our public markets are the best in the world for both businesses and investors.

Our country’s reputation as the gold standard for securities markets is due, in large part, to our emphasis on investor protection. Investor protection is often misunderstood as merely the prevention of fraud or other unethical conduct. While prevention is important, the concept of investor protection runs much deeper. If, for example, there is little public information about a company, it will be difficult and prohibitively expensive for investors—and especially retail investors—to confidently determine a value for the company’s shares or evaluate the risks presented by an investment in the company. By requiring robust disclosures, our laws protect investors by facilitating an efficient price discovery mechanism. This, in turn, bolsters confidence in our markets and makes people more willing to invest in job-creating enterprises. In this and many other ways, investor protection encourages capital formation.

Historically, public policy has favored the public markets over the private markets, where companies raise money through private offerings by taking advantage of exemptions from the registration and disclosure requirements. Unfortunately, as described below, we have seen a

<sup>8</sup> See [Joint Securities Law Professor Comment Letter](#) Regarding the SEC Concept Release on Harmonization of Securities Offering Exemptions (“Joint Professor Letter”) (Sept. 24, 2019) (“Any consideration of the regulatory web of transaction exemptions should begin with an acknowledgement that public securities markets, which are the product of SEC-registered offerings, remain the standard against which securities offerings and markets should be judged. Since the end of World War II, U.S. public securities markets have been the envy of the world in terms of size and liquidity and as engines for capital formation. This status owes not just to the economic might of the United States, but moreover to the legal architecture of federal securities laws, built over eight decades, which has protected investors.”)

monumental shift in recent years toward the private markets. In our view, the best way to revitalize our markets is to reinforce the time-tested fundamental bargain by which companies can enjoy broad access to investors in return for fulsome disclosure.<sup>9</sup> We encourage lawmakers to pursue policies that strengthen our public markets by enhancing efficiency, transparency, and a level playing field, rather than policies that pull companies and investors away from the public markets.

### B. Private Offerings Under Rule 506 Are Now Dominant

We, along with many other commentators,<sup>10</sup> are concerned that public offerings of securities are no longer the dominant form of capital formation in the United States. Over time, Congress and the SEC have expanded the ability of companies to raise large sums of capital privately and stay private longer, without providing the type of disclosure that is required for a public offering.

From the beginning of the federal securities laws, there have been exceptions to the general rule that offerings conducted in the United States must be registered with the SEC, and offerings meeting certain conditions have been exempted from mandatory disclosure requirements. The most notable of these exemptions was for offerings that did not involve a “public offering” of securities.<sup>11</sup> Conceptually, fulsome public disclosures were considered unnecessary when a sale of securities did not involve an offer to the public.<sup>12</sup>

Of course, this begs the question: what types of transactions do not involve a “public offering”? In a seminal case addressing this question, the Supreme Court in 1953 considered an offering to employees of the issuer and noted that “the number of offerees is not determinative of whether an offering is public.”<sup>13</sup> According to the Supreme Court, to be a transaction not involving a public offering, it must be directed to persons who “do not need the protection of

<sup>9</sup> See George S. Georgiev, [The Breakdown of the Public-Private Divide in Securities Law: Causes, Consequences, and Reforms](#), 18 N.Y.U. J.L. & Bus. 221, 240 (Fall 2021) (“Breakdown of the Public-Private Divide Paper”) (“On a conceptual level, becoming a public company entails a bargain: a heretofore private company gains access to large and highly liquid pools of public capital, which enables it to raise funds quickly, efficiently, and at low cost, but, in return, the company becomes subject to an extensive federal regulatory regime. The foundational rationale for this regime’s existence is the need to protect the ‘investing public’ — the investors, *i.e.*, suppliers of capital, who buy and sell securities on the public markets.”).

<sup>10</sup> See, *e.g.*, Joint Professor Letter; [Consumer Federation of America Comment Letter](#) Regarding the SEC Concept Release on Harmonization of Securities Offering Exemptions (“CFA Comment Letter”) at 9-13. See also Craig McCann, Susan Song, Chuan Qin & Mike Yan, [HJ Sims Reg. D Offerings: Heads, HJ Sims Wins - Tails, Their Investors Lose](#), SLCG Economic Consulting (2022). See also [Inactive and Delinquent Reg. D Issuers \(2022\)](#); [Regulation D Offerings Summary Statistics \(2022\)](#) and [Broker-Sold Regulation D Offerings Summary Statistics \(2022\)](#), all by Craig McCann, Chuan Qin & Mike Yan.

<sup>11</sup> Section 4(a)(2) of the Securities Act (formerly section 4(2) and, earlier, section 4(1)), 15 U.S.C. § 77d(4)(a)(2).

<sup>12</sup> See *SEC v. Ralston Purina Co.*, 346 U.S. 119, 122 (1953), citing H.R. Rep. No. 85, 73<sup>rd</sup> Congress, 1<sup>st</sup> Session.

<sup>13</sup> See *SEC v. Ralston Purina Co.*, 346 U.S. 119, 125 (1953).

the [Securities Act of 1933]" because they are able to "fend for themselves."<sup>14</sup> Further, in view of the broadly remedial purposes of the Securities Act, the Supreme Court held that it is reasonable to place on an issuer the burden of proving that purchasers of its securities had access to the kind of information which registration under the Securities Act would disclose.<sup>15</sup>

Using its exemptive authority, the Commission adopted Rule 506 of Regulation D in 1982.<sup>16</sup> In general, Rule 506 provided that sales of securities to unlimited numbers of accredited investors and up to 35 sophisticated non-accredited investors would not be considered a public offering that requires registration, but only if the offeror did not use any form of general solicitation. Accredited investors were defined as individuals with a net worth in excess of \$1,000,000 (either alone or together with a spouse) or an income of \$200,000 per year (or married couples with a combined income of \$300,000).

In 2011, Congress altered the calculation of net worth to remove a person's primary residence. However, the income and net worth thresholds have not otherwise been changed by Congress or the Commission since 1982. Given the effects of inflation, we note that an exemption that originally allowed unregistered securities to be sold to 1.6 percent of the U.S. population now allows those sales to approximately 13 percent of the population.<sup>17</sup>

Beyond the failure to adjust the accredited investor definition for inflation, Congress and the Commission have taken other steps to expand the scope of the exemption under Rule 506. Taken together, these steps have strayed well beyond an exemption that was specifically designed for transactions that do not involve a public offering. For example, the Commission long held that an offering limited to investors with a pre-existing substantive relationship with the issuer would not involve a public offering, but over the years the Commission has made it easier and easier for a company to establish such relationships with prospective investors. It is now possible to utilize a broad internet-based solicitation to establish a purported "relationship" with a wide range of prospective investors and then use that relationship to avoid the prohibition on general solicitation in subsequent securities offerings.<sup>18</sup> Another major development was in 2013 when the Commission adopted Rule 506(c) to satisfy a mandate imposed by Congress in the 2012 JOBS Act. Rule 506(c) provides that a company can broadly solicit and generally advertise an offering and still be deemed in compliance with the exemption of Rule 506, so long as the company takes steps to verify that all investors are

<sup>14</sup> *Id.* at 124-25.

<sup>15</sup> *Id.* at 126-27.

<sup>16</sup> SEC, Revision of Certain Exemptions from Registration for Transactions Involving Limited Offers and Sales, Release No. 33-6389, 47 FED. REG. 51 (Mar. 16, 1982).

<sup>17</sup> SEC Proposed Rule, [Amending the "Accredited Investor" Definition](#) ("Proposed Accredited Investor Definition"), Release Nos. 33-10734 and 34-87784 (Dec. 18, 2019), at 77, 134.

<sup>18</sup> Stephen Quinlivan, [SEC Explains How to Form a Pre-Existing Relationship Using the Internet; New CDI's Issued](#), [Stinson Corporate & Securities Law Blog](#) (Aug. 7, 2015).

accredited investors.<sup>19</sup> More recently, the Commission adopted amendments classifying certain individuals as accredited investors by virtue of their “sophistication,” without regard to their financial wherewithal.<sup>20</sup>

In 1996, the National Securities Markets Improvement Act (“NSMIA”)<sup>21</sup> preempted state regulation of Rule 506 offerings. Thereafter, companies were allowed to raise unlimited amounts of capital from unlimited numbers of accredited investors with no specific disclosure obligations and no regulatory review at either the federal or state level. This also had the effect of dis-incentivizing companies from pursuing exchange listings in order to avail themselves of exemptions available under state law for exchange-listed securities.

Originally, the purchaser of a security in an offering under Rule 506 was restricted from reselling it for a period of two years.<sup>22</sup> In 1997, the holding period was shortened to one year, if certain conditions were met, and the conditions were removed in 2007.<sup>23</sup> Then, in 2015, a provision of the FAST Act allowed immediate resale of restricted securities to other accredited investors, a designation which now applies to a sizable portion of the overall investing public. Together, these changes dramatically reduced the need for companies to turn to the public markets in order to provide a way for founders, early investors, and employees to sell their shares. Moreover, the changes made it far more likely that unregistered securities would be widely distributed to the general public.<sup>24</sup>

In summary, the exemption in Rule 506 was intended to allow sales to a limited number of people who were able to “fend for themselves” and did not need the protections inherent in the registration requirements because they possessed the bargaining power or financial wherewithal to overcome the normal informational asymmetries between buyers and sellers of securities.<sup>25</sup> However, the exemption no longer meaningfully limits offerings to this type of person, and the conditions on this exemption for “non-public offerings” have nothing to do with the size, economic importance, or disparate ownership of the company.

As a result of these developments, what was meant as an exception to the general rule has become the primary means of raising capital in this country. A 2020 study of Regulation D by the SEC revealed that, in the preceding decade, there had been a steady increase in the number

<sup>19</sup> See SEC, [Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings: A Small Entity Compliance Guide](#) (last modified Sept. 20, 2013).

<sup>20</sup> See SEC Final Rule, [Accredited Investor Definition](#), Release Nos. 33-10824 and 34-89669 (Aug. 26, 2020).

<sup>21</sup> Pub. L. No. 104-290, 110 Stat. 3416 (1996).

<sup>22</sup> See [Letter from Keith F. Higgins](#), Chair, Committee on Federal Regulation of Securities, American Bar Association, to John W. White, Director, SEC Division of Corporation Finance (Mar. 22, 2007).

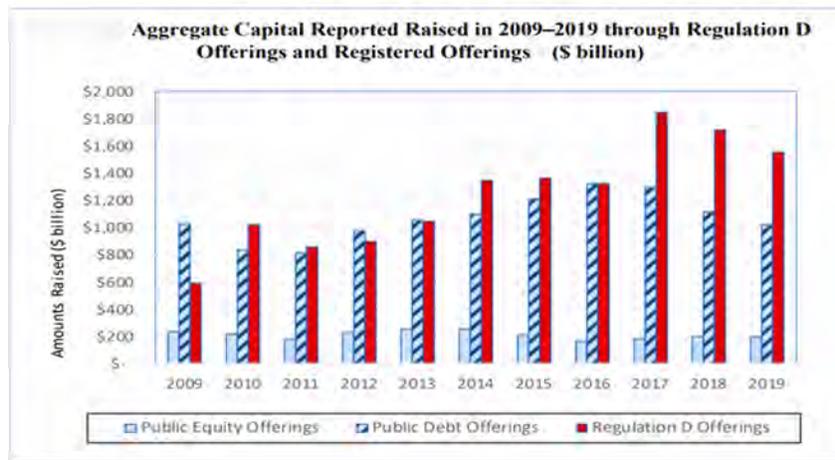
<sup>23</sup> See Renee M. Jones, [The Unicorn Governance Trap](#), 66 U. PA. L. REV. ONLINE 165 (2017).

<sup>24</sup> *Id.* The FAST Act created a new Section 4(a)(7) under the Securities Act, which preempted state law to facilitate secondary trading by establishing a nonexclusive safe harbor for private resales under the so-called “Section 4(a)(1½)” exemption.

<sup>25</sup> See CFA Comment Letter at 9-13.

of offerings and amounts raised in Rule 506 offerings. As shown in Table 1, Regulation D offerings—99.9 percent of which are under Rule 506—have eclipsed the amounts raised in public offerings.<sup>26</sup>

Table 1



Source: SEC Reg A/Reg D Report.

The growing dominance of the private markets has systemic implications. Specific disclosures are not mandated under Rule 506, and voluntary disclosures are often tainted with inaccuracies or overly optimistic projections that lead to mispricing of the securities. Even the most sophisticated investors often lack the information needed to make informed investment decisions, and this can lead to market-wide bubbles that cause widespread harm when they burst. Additionally, founder-friendly terms that are common in private offerings can lead to weak corporate governance and internal controls, making fraud or other misconduct more likely. Other stakeholders, such as companies in the issuer's supply chain, also suffer from the lack of public disclosure because it is more difficult to assess the risk of their commercial partners. In turn, the supplier's own disclosures may become inaccurate or misleading. Furthermore, regulators lack a line of sight into these markets, so their rulemaking, examination, enforcement, and education work suffers. As the private market continues to

<sup>26</sup> Regulation D includes a second exemption under Rule 504, but Rule 506 offerings make up more than 99.9 percent of offerings conducted under Regulation D. See SEC, [Report to Congress on Regulation A / Regulation D Performance As Directed by the House Committee on Appropriations in H.R. Rept. No. 116-122](#) ("SEC Reg A/Reg D Report") (Aug. 2020) at 16.

expand, these and other consequences undermine responsible capital formation generally, and the virtues of fairness and efficiency that undergird our public markets become fleeting.

### C. The 2012 JOBS Act Did Not Achieve Its Goals for the Public Markets

It is clear from its legislative history that Congress intended for the 2012 JOBS Act to incentivize more companies to enter the public markets. Members of Congress took steps to address what some saw as the deterioration of the public markets, pointing to the slackening pace of IPOs and the decline in the number of companies listed on exchanges which, in turn, yielded fewer attractive investment opportunities for retail investors. To curb this trend, Title I of the 2012 JOBS Act created a new “IPO on-ramp” to reduce the perceived burdens of becoming a public company and thereby encourage more companies to conduct an IPO.

Title I of the 2012 JOBS Act lowered a number of the requirements for an “emerging growth company” (“EGC”) to become a public company. An EGC was defined as a company with total annual gross revenues of less than \$1 billion in its most recent fiscal year—a definition that would have encompassed the vast majority of companies that had gone public before the 2012 JOBS Act.<sup>27</sup> EGCs were allowed to go public while disclosing two prior years of audited financial statements instead of three, and EGCs were exempted from the requirement to disclose executive compensation for five years following the IPO. Title I also allowed EGCs to “test the waters” by communicating with investors prior to the launch of an IPO, eliminated firewalls that prevented research analysts from communicating with their own firm’s IPO bankers and their bank’s IPO clients, and allowed companies to seek confidential review by SEC staff of draft registration statements prior to making them available to the public. Following an IPO, and for as long as the company maintains its EGC status (up to five years), the company remains exempt from mandatory audit firm rotation and is not subject to auditor attestation under Section 404 of the Sarbanes-Oxley Act of 2002.<sup>28</sup>

Although the 2012 JOBS Act included the IPO on-ramp to encourage companies to enter our public markets, the remainder of the legislation contained provisions that ran counter to that purpose. Instead of attempting to stem the rising tide of exempt offerings, the 2012 JOBS Act made it even easier for companies to raise unlimited amounts of capital in the private markets and forestall indefinitely the need to become a public reporting company. In Title II, Congress eliminated the longstanding prohibition against the use of general solicitation by those who engage in private offerings under Rule 506, as described above. Title III created a new exemption to allow companies to raise capital through “crowdfunding”—selling small amounts of securities to large numbers of investors—and Title IV directed the SEC to expand the ability of companies to raise capital under Regulation A. All three of these titles allowed companies

<sup>27</sup> Lori Schock, Director, SEC Office of Investor Education and Advocacy, [Remarks at InvestEd 2012 Conference: Outline of Dodd-Frank Act and JOBS Act](#) (June 9, 2012).

<sup>28</sup> 2012 JOBS Act at §§ 102-108.

to, in effect, raise money from the general public without having to produce critical initial disclosures and periodic reports that are the hallmark of public companies.

Titles V and VI of the 2012 JOBS Act altered Section 12(g) of the Securities Exchange Act of 1934 (“Exchange Act”). Prior to these changes, Section 12(g) required companies to become public reporting companies, regardless of the method used to distribute the shares, if they had assets of \$10 million and a class of securities that were “held of record” by at least 500 persons.<sup>29</sup> According to the SEC, “the registration requirement of Section 12(g) was aimed at issuers that had ‘sufficiently active trading markets and public interest and consequently were in need of mandatory disclosure to ensure the protection of investors.’”<sup>30</sup> Title V of the 2012 JOBS Act raised this threshold to 2,000 total shareholders or 500 non-accredited shareholders, excluding those who received shares as part of an employee compensation plan. Title VI made similar changes for banks and bank holding companies.<sup>31</sup>

Limiting the thresholds in Section 12(g) to shares “held of record” has a significant impact. A shareholder of record is one who holds official title to the shares, but that shareholder could be an entity such as a brokerage firm or private fund that holds securities on behalf of numerous beneficial owners who hold the contractual right to sell or vote the shares.<sup>32</sup> As a practical matter, then, the new thresholds have given companies the ability to stay private indefinitely, no matter how widely held and widely traded their shares.<sup>33</sup>

The impacts of the 2012 JOBS Act have been decidedly mixed in large part because the legislation pursued contradictory goals. Nevertheless, two things are apparent: (1) as shown above in Table 1, exempt offerings have continued their astronomical growth,<sup>34</sup> and (2) as shown below in Table 2, the legislation was not successful in getting more companies to

<sup>29</sup> Usha Rodrigues, [The Once and Future Irrelevancy of Section 12\(g\)](#), 2015 U. ILL. L. REV. 1529, 1530.

<sup>30</sup> SEC, Reporting by Small Issuers, Release No. 23,407, 1986 WL 703825 at \*2 (July 8, 1986). See also Anat Alon-Beck, [Mythical Unicorns and How to Find Them: The Disclosure Revolution](#), Columbia Business Law Review (2022 Forthcoming), Case Western Reserve University Research Paper Series in Legal Studies, Paper No. 2022-6, at 22 (“Disclosure Revolution Paper”) (“The original intent behind instituting limits on shareholders of record was to capture firms which [were] already broadly trading.”).

<sup>31</sup> SEC, [Changes to Exchange Act Registration Requirements to Implement Title V and Title VI of the JOBS Act: A Small Entity Compliance Guide](#) (May 24, 2016).

<sup>32</sup> See [NASAA Letter to Congress](#) in Support of Reed Amendment #1931 (Mar. 22, 2012).

<sup>33</sup> Contrary to the claims of 2012 JOBS Act proponents, a subsequent analysis of IPOs between June 1, 2000, and May 16, 2013, revealed that only 2.6 percent of those companies were approaching the 500 shareholder limit in Section 12(g). According to Professor Usha Rodrigues, who conducted the study, “the post-JOBS Act Section 12(g) will be unlikely to affect more than a handful of firms.” This means that what was already a weak mechanism for ushering private companies to the public markets has been rendered virtually meaningless. See Disclosure Revolution Paper at 5 (Section 12(g) “was amended in 2012 via the Jumpstart Our Business Startups Act (“JOBS Act”) to remove what little regulatory teeth it had left.”).

<sup>34</sup> Table 1 reflects the usage of only one alternative to public offerings—offerings that are exempt from registration under Rule 506. For details regarding the usage of other exemptions, including Regulation A and Regulation Crowdfunding, see SEC Reg A/Reg D Report and [SEC Staff Report to the Commission Regarding Regulation Crowdfunding](#) (June 18, 2019).

conduct IPOs.<sup>35</sup> We encourage the current Congress, before pursuing a JOBS Act 4.0, to objectively examine the impacts of the 2012 JOBS Act and particularly the unintended consequences it has had on the public markets.

Table 2



Source: Tim Fries, [Despite Pandemic, 2020 Saw 450 IPOs Raise Over \\$156 Billion](#), The Tokenist (Dec. 14, 2020).

Table 2 reveals that the volume of IPOs did not increase significantly after the “IPO on-ramp” took effect in 2012. IPO volumes in 2013 and 2014 were higher, but the subsequent declines suggest that IPO volumes are largely attributable to economic conditions rather than the passage of the IPO on-ramp. Even more recently, the number of IPOs has increased substantially in 2020 and 2021, but those increases are driven overwhelmingly by the explosion in the proliferation of Special Purpose Acquisition Companies (“SPACs”).<sup>36</sup>

Since the adoption of the 2012 JOBS Act, several academic studies have been conducted to examine its effects. In short, the academic findings show that the 2012 JOBS Act failed to

<sup>35</sup> One notable exception has been found in the biotech industry, a major proponent of the JOBS Act. An analysis by Craig Lewis and Josh White showed that “annual biotech IPO volume from 2012 to 2018 increased by 219 percent over a similar period before the JOBS Act. Moreover, biotech companies account for just under 40 percent of all IPOs in the U.S. after the JOBS Act.” Craig Lewis & Josh White, [Deregulating Innovation Capital: The Effects of the JOBS Act on Biotech Startups](#), Review of Corporate Finance Studies (forthcoming) (Nov. 13, 2022).

<sup>36</sup> See Jay R. Ritter, [Special Purpose Acquisition Company \(SPAC\) IPOs Through 2021](#) (July 14, 2022). NASAA generally supports rules to encourage companies to bring their securities to the public market through registered offerings. We have expressed concerns regarding the use of SPACs and have supported a number of SEC proposals to address those concerns. See, e.g., [NASAA Comment Letter to SEC Regarding File No. S7-13-22: Special Purpose Acquisition Companies, Shell Companies, and Projections](#) (June 13, 2022).

NASAA REPORT AND RECOMMENDATIONS FOR REINVIGORATING OUR CAPITAL MARKETS

reduce costs of issuance and lead to a sustained recovery in IPO activity. The following quotations illuminate the research findings:

We examine the effects of Title I of the Jumpstart Our Business Startups Act for a sample of 312 emerging growth companies (EGCs) that filed for an initial public offering (IPO) from April 5, 2012 through April 30, 2015. We find no reduction in the direct costs of issuance, accounting, legal, or underwriting fees for EGC IPOs. Underpricing, an indirect cost of issuance that increases an issuer's cost of capital, is significantly higher for EGCs compared to other IPOs. More importantly, greater underpricing is present only for larger firms that are newly eligible for scaled disclosure under the Act. Overall, we find little evidence that the Act in its first three years has reduced the measurable costs of going public.... [Our] results are consistent with a large body of literature that shows that investors value transparency and, in its absence, issuers are penalized by lower prices for their securities.

Susan Chaplinsky, Kathleen Weiss Hanley & S. Katie Moon  
[The Jobs Act and the Costs of Going Public](#)  
*Journal of Accounting Research*, Vol. 55, No. 4 (2017)

The Jumpstart Our Business Startups (JOBS) Act has not led to a sustained recovery in IPO activity, but to poorer-quality firms raising public equity. Firms going public under the Act are largely cash-starved, pay dearly to raise equity, and often rely on further public issues to avert financial distress. Proceeds raised are used to do more hiring, repay debt, and boost executive pay, but not to increase investments. Many firms lose exemptions sooner than allowed by the Act, whereupon they face higher compliance costs. The JOBS Act has not revived public equity markets and may have even undermined their attractiveness.

Anantha Divakaruni & Howard Jones  
[Can Lowering the Bar Revive Public Markets? Evidence from the JOBS Act](#)  
 Aug. 28, 2020

EGCs have both lower financial performance and a lower Tobin's Q-ratio [(the ratio of a company's equity market value to its book value)] compared to the financial performance and Tobin's Q-ratio of non-EGCs. Moreover, the value relevance of accounting information for EGCs is lower than the value relevance of accounting information for non-EGCs. This study contributes to the accounting regulation literature by documenting the inferior market performance and financial information quality of EGCs, i.e., the unintended consequences of the JOBS Act.

Ji Yu, Zabiollah Rezaee & Joseph H. Zhang  
[The Accounting and Market Consequences of the JOBS Act of 2012: An Early Study](#)  
 27 *Asian Review of Accounting* 49 (2019)

## NASAA REPORT AND RECOMMENDATIONS FOR REINVIGORATING OUR CAPITAL MARKETS

[The JOBS Act] was designed to reduce IPO costs by allowing eligible firms to test the waters with investors and reduce disclosure, both of which increase firms' information advantage over investors. We model firm behavior in response to this increased information advantage and using a difference-in-difference setting, we show that while these changes have benefited some firms, they have led to a decrease rather than an increase in the number of firms going public.

Michelle Dathan & Yan Xiong  
[Too Much Information? Increasing Firms' Information Advantages in the IPO Process](#)  
 April 7, 2022

The JOBS Act allows certain analysts to be more involved in the IPO process but does not relax restrictions on analyst compensation structure. We find that these analysts initiate coverage that is more optimistically biased, less accurate, and generates smaller stock market reactions. Investors purchasing shares following these initiations lose over 3% of their investment by the firm's subsequent earnings release. By contrast, issuers, analysts, and investment banks appear to benefit from this increased bias, as optimism is more positively associated with proxies for firm visibility and investment banking revenues when analysts are involved in the IPO process.

Michael Dambra, Laura Casares Field, Matthew T. Gustafson & Kevin Pisciotta  
[The Consequences to Analyst Involvement in the IPO Process: Evidence Surrounding the JOBS Act](#)  
 65 Journal of Accounting & Economics 302 (April-May 2018)

Thanks to the increase in Section 12(g) thresholds and the easing of exempt capital raising restrictions under Regulation D, it is far easier for companies to stay private longer and grow to staggering sizes. Using our hand-collected data from public filings with the Securities and Exchange Commission ("SEC"), we have found the average number of shareholders of record in unicorn IPOs has nearly doubled in the decade since the passage of the JOBS Act. Valuations for unicorn IPOs have continued to soar higher every year.

Anat Alon-Beck  
[Mythical Unicorns and How to Find Them: The Disclosure Revolution](#)  
 Columbia Bus. L. Rev. (2022 Forthcoming)  
 Case Western Reserve Univ. Research Paper Series in Legal Studies, Paper No. 2022-6, at 5

Title I of the Jumpstart Our Business Startups (JOBS) Act provides newly public firms broad-scale regulatory relief but limits the benefits to a certain subset of firms named "Emerging Growth Companies (EGCs)." One of the EGC criteria is based on a \$700 million public float threshold. We find evidence that firms appear to bunch up their public float at IPO issuances below the \$700 million threshold and repurchase their shares after the issuances to be eligible for the EGC status. Firms staying below the threshold are more likely to substitute public equity with debt. We further find that the leverage effect persists over time (the leverage ratchet effect) even when EGCs lose their status.

Khaled Alsbah & Katie Moon  
 IPO Regulation and Initial Capital Structure: Evidence from the JOBS Act  
 July 14, 2020

NASAA urges Congress to consider these academic findings as it evaluates whether and how to advance legislation during the 118<sup>th</sup> Congress. Moreover, as explained in greater detail in Part IV of this report, NASAA urges Congress to require and fund a comprehensive study on public and private markets led by the SEC's Division of Economic and Risk Analysis. Agency staff could use these academic papers to inform their work on the comprehensive study.

#### **D. The Current Incentives to Go Public Are Minimal**

The growing dominance of the private markets over the public markets was well underway by the time the 2012 JOBS Act was enacted. Congress could have chosen to reverse these trends by tightening the exemptions from the securities registration requirements, thereby nudging more companies into the public sphere. Instead, it chose a counterproductive solution to the problem. In what could fairly be described as a proverbial race to the bottom, Congress attempted to grow both the public and private markets at the same time by expanding exemptions—rather than tightening them—while reducing the disclosure requirements for public companies.

As described above, the federal securities laws originated with a simple bargain: disclosure in exchange for investors.<sup>37</sup> A company was expected to disclose substantial amounts of information in return for the ability to solicit members of the general public, and a company was required to enter the public sphere if it attracted a large shareholder base. There were substantial benefits to becoming a public company because a private company wishing to raise capital faced many barriers, including a prohibition on advertising and severe limitations on resales of the securities.

<sup>37</sup> Elisabeth de Fontenay, [The Deregulation of Private Capital and the Decline of Public Companies](#), 68 HASTINGS L.J. 445, 447-48 (2017) ("Deregulation of Private Capital Paper").

This disclosure bargain has largely been eliminated.<sup>38</sup> There are now few benefits to becoming a public company because Congress and the SEC have expanded exemptions to the point that they include few meaningful barriers, and a company can raise capital from broad swaths of investors in offerings that are exempt from registration. Indeed, in some instances, issuers have successfully raised funds from more than 1,000 investors in “non-public” offerings under Rule 506.<sup>39</sup> Investors in these offerings receive little or no disclosure about the company, and the company may find that moving from this environment into the daylight of the public markets can be difficult. WeWork, for example, had little difficulty finding investors in the private market, but its IPO imploded when details about its corporate governance and financial condition were exposed to the public.<sup>40</sup>

For decades now, Congress and the SEC have lowered investor protections in both the public and private markets in pursuit of contradictory policy goals. On the one hand, policymakers have tried to incentivize companies to go public by lowering the regulatory burdens and costs associated with being a public company. At the same time, however, the steady expansion of exemptions has wiped away the disadvantages of staying private, and there is relatively little burden or cost associated with exempt offerings. In this environment, it should be no surprise that more companies are choosing to stay private longer, and it is predictable that further efforts to incentivize companies to go public by reducing regulatory burdens are unlikely to work.

Despite this predictable result, the JOBS Act 4.0 contains provisions that unfortunately would continue the race to the bottom by, for example, trying to attract more companies to go public by extending EGC status to 10 years, among other things, while making it easier for companies to raise capital through exempt offerings and stay private longer. This mix of public market incentives in the form of weakened regulatory requirements and private market expansions will logically have the same result as the 2012 JOBS Act; namely, the public markets will continue to suffer while the private markets expand yielding no benefit to public capital formation.

In our view, efforts to revitalize U.S. capital markets for the benefit of companies, investors, and the overall economy should focus on restoring the primacy of the public markets. This will necessarily involve a reconsideration of the exemptions from registration, especially Rule 506 and the definition of an accredited investor, as well as a restoration of a meaningful threshold in Section 12(g) whereby large companies are pushed into the public markets.

---

<sup>38</sup> *Id.*

<sup>39</sup> See, e.g., [Form D filing for PE Premier Blackstone Strategic Partners VIII Onshore Feeder LP](#) or [PE Premier Blackstone Life Sciences V Onshore Feeder LP](#). These are their initial Form D notice filings. There may be many more investors who were acquired after the initial filing.

<sup>40</sup> See, e.g., Rani Molla & Shirin Ghaffary, [The WeWork Mess, Explained](#), VOX (Oct. 22, 2019).

## II. Helping Small Businesses and Entrepreneurs

Early-stage companies, and especially the truly Main Street businesses that state regulators are most focused upon, need options to raise seed capital and fund the early growth of their companies. Several options currently exist, and they have been expanded recently by states, Congress, and the SEC in the hopes of jumpstarting capital formation.

Regulation A has two offering tiers: Tier 1, for offerings of up to \$20 million in a 12-month period; and Tier 2, for offerings of up to \$75 million in a 12-month period.<sup>41</sup> There are certain basic requirements applicable to both Tier 1 and Tier 2 offerings, including company eligibility requirements, bad actor disqualification provisions, disclosure, and other matters. Additional requirements apply to Tier 2 offerings, including limitations on the amount of money a non-accredited investor may invest in a Tier 2 offering, requirements for up to two years of audited financial statements, and the filing of ongoing reports.<sup>42</sup> Issuers in Tier 2 offerings are not required to register or qualify their offerings with state securities regulators, and issuers seeking less than \$20 million can elect to proceed under either Tier 1 or Tier 2.<sup>43</sup>

Issuers may also raise capital through state crowdfunding laws or the federal regime that in many respects borrowed from state laws. Federal Regulation Crowdfunding currently allows a company to raise up to \$5 million in a 12-month period, and all transactions must take place online through an SEC-registered funding portal or broker-dealer. The issuer must disclose specified information about the business, and if the issuer is a first-time user of Regulation Crowdfunding, this includes two years of financial statements that are reviewed by a public accountant but not audited.<sup>44</sup>

As described above, small businesses and entrepreneurs can also take advantage of the exemption available under Rule 506 of Regulation D.<sup>45</sup> Issuers can raise an unlimited amount from accredited investors with no specific disclosure requirements. Issuers can also sell securities to as many as 35 sophisticated non-accredited investors, provided the issuer does not

<sup>41</sup> 17 C.F.R. §§ 230.251 et seq.

<sup>42</sup> See, e.g., SEC, [Amendments to Regulation A: A Small Entity Compliance Guide](#) (revised Feb. 4, 2019).

<sup>43</sup> The states, under the auspices of the NASAA, have created coordinated review protocols for Tier 1 offerings. Coordinated review programs for state registration of securities or franchise offerings streamline the process for an issuer seeking to undertake a multi-state registration of its securities or franchise offering. In addition to establishing uniform review standards, coordinated review is designed to expedite the registration process, saving the issuer time and money. Coordinated review is voluntary, and there is no additional cost for choosing to register an offering through coordinated review. For more information, visit NASAA's Coordinated Review website: [coordinatedreview.org](http://coordinatedreview.org).

<sup>44</sup> 17 C.F.R. §§ 227.100 et seq.

<sup>45</sup> 17 C.F.R. § 230.506.

use general solicitation<sup>46</sup> and provides the non-accredited investors with the same type of information that is available to investors under Regulation A.<sup>47</sup>

### A. Regulation A and Regulation Crowdfunding Cannot Compete with Regulation D

In August 2020, the SEC issued a report—as mandated by Congress—on the performance of Regulation A and Regulation D. In the report, Commission staff examined Regulation A offerings conducted between June 2015, when the exemption was expanded pursuant to the 2012 JOBS Act, and the end of 2019.<sup>48</sup> During this time period, the total amount raised under Regulation A was \$2.4 billion, including \$2.2 billion under Tier 2 and \$230 million under Tier 1.<sup>49</sup> Issuers sought an average of \$30.1 million in Tier 2 offerings, but raised on average only \$15.4 million. In Tier 1 offerings, issuers sought an average of \$7.2 million and raised \$5.9 million.<sup>50</sup> Data is not available to show the extent to which retail investors other than accredited investors were participants in these offerings.

The Commission staff found that the typical issuer does not experience an improvement in profitability, continuing to realize a net loss in the years following an offering that utilizes Regulation A. This was based on available data, which necessarily overstated the success rate because it only included issuers that continued to file periodic reports after the offerings and not those that ceased operations and reporting.<sup>51</sup> And despite the infusion of investor capital, only 45.8 percent of issuers continued filing periodic reports for three years following the offering.<sup>52</sup>

Regulation Crowdfunding has produced even more modest results. In June 2019, the Commission staff undertook a study on the impacts of Regulation Crowdfunding. The study found that during the reviewed period, from May 16, 2016, through December 31, 2018, issuers raised a total of \$107.9 million under Regulation Crowdfunding.<sup>53</sup> Of the offerings that were reported completed, the average offering sought a maximum amount of \$577,385 and raised

<sup>46</sup> 17 C.F.R. § 230.506(c).

<sup>47</sup> 17 C.F.R. § 230.502.

<sup>48</sup> SEC Reg A/Reg D Report.

<sup>49</sup> *Id.* at 91.

<sup>50</sup> *Id.* at 88-89.

<sup>51</sup> *Id.* at 94.

<sup>52</sup> *Id.* at 98.

<sup>53</sup> SEC, [Staff Report to the Commission Regarding Regulation Crowdfunding](#) (June 18, 2019) (“SEC Crowdfunding Report”) at 4.

an average of \$208,300 (with a median of \$107,367), well below the \$1.07 million offering size that was permissible under Regulation Crowdfunding at that time.<sup>54</sup>

According to academic researchers, crowdfunding can provide access to capital for small businesses that are not usually served by angel investors and venture capital firms.<sup>55</sup> Regulation Crowdfunding may be appealing, for example, to a business whose loyal customers want to support the business by investing in it. On the other hand, it appears that many small businesses utilize crowdfunding because they are unable to attract funding from traditional angel or venture capital sources, leaving them with no other options. The equity crowdfunding market faces severe adverse selection, meaning that the least promising firms are likely to utilize the exemption, and this limits the appeal of these offerings. Moreover, relative to angel-backed firms, crowdfunded firms are less likely to progress through additional stages of financing that ultimately provide an exit to investors.<sup>56</sup>

Offerings under Regulation A and Regulation Crowdfunding have experienced modest growth in recent years, but those gains are eclipsed by the explosive growth of offerings under Rule 506. Rule 506 offerings continue to raise 1,000 times more capital than Regulation A and Regulation Crowdfunding combined, and it is hard to imagine that the other exemptions will ever compete with Rule 506. Regulation A and Regulation Crowdfunding, sometimes considered “quasi-private offerings,” require specific disclosures that are not required under Rule 506, and this can make them less appealing from the perspective of issuers. Rule 506 sales must be made primarily to accredited investors, but this is not a significant impediment for founders of start-ups who generally prefer to raise large amounts of money from a few investors rather than small amounts from many investors. Further, given the growth of the number of issuers using Rule 506 and the amount of capital raised, it is clear that this market is in need of neither investors nor capital.

Given the ease with which funds can be raised under Rule 506, promising companies will continue to choose it, and the less attractive early-stage companies will be left to the retail investors in offerings under Regulation A and Regulation Crowdfunding. Unless policymakers are willing to place additional restrictions on Rule 506, and thereby encourage more promising early-stage businesses to use Regulation A or Regulation Crowdfunding, offerings utilizing those exemptions will remain unappealing and continued efforts to expand the exemptions will not work.

<sup>54</sup> *Id.* at 3. Despite the modest usage of the exemption, the Commission expanded the allowable offering size to \$5 million in 2020. See SEC Final Rule, [Facilitating Capital Formation and Expanding Investment Opportunities by Improving Access to Capital in Private Markets](#), Release No. 33-10884 (Nov. 2, 2020) (“SEC Harmonization Rule”).

<sup>55</sup> Iman Dolatabadi, Cesare Fracassi & Lin Yang, [Equity Crowdfunding in the U.S.](#) (Oct. 1, 2021).

<sup>56</sup> *Id.*

## B. Companies Need a Stronger Public Market, Not More Ways to Stay Private

At this point, when it comes to capital formation, what small companies need most is a healthy public market to grow into, and the further expansion of exemptions will defeat this purpose. This is a lesson of the 2012 JOBS Act, which stripped away important investor protections in an effort to induce more companies to enter the U.S. public markets. As described above, the number of IPOs did not increase, in part because the 2012 JOBS Act undercut its own goal by expanding the options to remain private. Consequently, more money is now raised under Rule 506 than in public offerings, and promising U.S. tech companies are now staying private an average of 11 years before an IPO as opposed to the 7.8 year average before the 2012 JOBS Act took effect.<sup>57</sup> If this trend continues, the only companies in our public markets will be corporate behemoths long past their growth stage.<sup>58</sup>

The JOBS Act 4.0 contains the same internal inconsistency as the 2012 JOBS Act—for instance, compare “Title I. Encouraging Companies to be Publicly Traded” with “Title II. Improving the Market for Private Capital.” In effect, the bill perpetuates a flawed approach to capital formation by stripping away additional investor protections to spur IPO activity, then it undermines that goal by expanding opportunities for companies to stay private indefinitely. Predictably, the new JOBS Act 4.0 is likely to produce the same disappointing results.

Again, before pursuing a new JOBS Act 4.0, we urge Congress to undertake an objective review of the impacts on our capital markets from the 2012 JOBS Act. We also urge Congress to require an SEC study of our capital markets, including the utility of the various exemptions for capital formation by operating companies, the growth of the private markets vis-à-vis the public markets, and ways to reinvigorate the public markets. After reviews of this nature, we are confident that Congress will see the need for a different approach to helping small businesses. In our view, all market participants, including the start-ups and other small businesses in our states, would be best served by a rebalancing that returns us closer to the original principles of the securities laws, where “firms that chose to ‘go public’ took on substantial disclosure

<sup>57</sup> See Breakdown of the Public-Private Divide Paper.

<sup>58</sup> See Speech, SEC Commissioner Allison Herron Lee, [Going Dark: The Growth of Private Markets and the Impact on Investors and the Economy](#) (Oct. 12, 2021) (“Current estimates vary, but generally put the number of Unicorns worldwide at roughly 900, up from an estimated 39 in 2013. The list now includes not just Unicorns (those with an estimated valuation of at least \$1 billion) but also so-called “Decacorns” (estimated valuations of \$10 billion) and even “Hectocorns” with valuations approaching and exceeding \$100 billion. Although some of these large firms are subject to industry-specific regulation, such regulation does little to address financial transparency, and may be quite sparse (as with the growing number of crypto-related Unicorns).”).

burdens, but in exchange were given the exclusive right to raise capital from the general public.”<sup>59</sup>

### C. Preemption Harms Small Business Capital Formation

State securities regulators have a strong record of leadership in protecting retail investors and taking enforcement actions when unscrupulous activities would undermine responsible capital formation. Consider, for example, our recent record in matters involving digital assets. About a decade ago, NASAA began warning investors about scams tied to digital assets.<sup>60</sup> The first state enforcement actions against a fraudulent digital asset scheme occurred soon thereafter when state regulators issued orders to stop an initial coin offering (“ICO”) by BitConnect. This work evolved into Operation Cryptosweep, which was a task force comprised of U.S. and Canadian NASAA members who produced significant enforcement results related to ICOs and other cryptocurrency-related investment products.<sup>61</sup> Most recently, state regulators have been at the forefront of cases involving the unregistered offerings of securities in the form of interests in so-called crypto-lending programs like those offered by BlockFi, Celsius, and Voyager.<sup>62</sup> The harms we are currently encountering in the digital asset space undoubtedly would be worse if the federal government had to act alone.<sup>63</sup>

<sup>59</sup> Deregulation of Private Capital Paper at 451.

<sup>60</sup> See NASAA, Informed Investor Advisory: Virtual Currency (Apr. 2014). For additional NASAA advisories, see, e.g., Informed Investor Advisory: Decentralized Finance (DeFi) Defined (Dec. 6, 2021); Informed Investor Advisory: Protecting Your Online Accounts (Sept. 16, 2021); Informed Investor Advisory: Social Media, Online Trading and Investing (Apr. 1, 2021); Informed Investor Advisory: Initial Coin Offerings (Apr. 16, 2018); Informed Investor Advisory: Cryptocurrencies (Apr. 13, 2018); Informed Investor Advisory: The Next Big Thing (Nov. 9, 2015). [Access NASAA's Investor Advisories.](#)

<sup>61</sup> See, e.g., NASAA, [Operation Cryptosweep Results as of 2018](#). Upon the indictment of the founder of BitConnect in 2022, the U.S. Department of Justice (“DOJ”) described the ICO as a “massive cryptocurrency scheme” that defrauded investors of more than \$2 billion. See DOJ, [Founder of Fraudulent Cryptocurrency Charged in \\$2 Billion BitConnect Ponzi Scheme](#) (Feb. 25, 2022).

<sup>62</sup> See, e.g., [NASAA Letter to Congress](#) Regarding the Digital Commodities Consumer Protection Act of 2022 (Sept. 9, 2022); [Written Testimony of NASAA President and Maryland Securities Commissioner Melanie Senter Lubin Delivered to the U.S. Senate Committee on Banking, Housing, and Urban Affairs](#) (July 28, 2022); [NASAA and SEC Announce \\$100 Million Settlement with BlockFi Lending, LLC](#) (Feb. 14, 2022).

<sup>63</sup> See, e.g., Alex Nguyen, Cryptocurrency Firm FTX, Billionaire CEO Focus of Texas Securities Investigation, The Texas Tribune (Oct. 17, 2022); Francis Yue, ‘I Just Wake Up and Cry’: Voyager and Celsius Bankruptcies Have Destroyed Some Crypto Investors’ Confidence in Centralized Platforms, MarketWatch (July 15, 2022); Maria Ponnezhath and Tom Wilson, Major Crypto Lender Celsius Files for Bankruptcy, Reuters (July 14, 2022); Cheyenne Ligon, Texas, Other States Open Investigation Into Celsius Network Following Account Freeze (June 16, 2022); Five States File Enforcement Actions to Stop Russian Scammers Perpetrating Metaverse Investment Fraud (May 11, 2022); Sand Vegas Casino Club Located in the Metaverse Is Soliciting Investors to Invest Real Money in Un-Registered Investments (Apr. 13, 2022); New Jersey Bureau of Securities Orders Cryptocurrency Firm Celsius to Halt the Offer and Sale of Unregistered Interest-Bearing Investments (Sept. 17, 2021). See also NASAA Reveals Top Investor Threats for 2022 (Jan. 10, 2022); NASAA Announces Top Investor Threats for 2021 (Mar. 3, 2021); NASAA Announces Top Investor Threats for 2020 (Dec. 23, 2019).

As the recent implosions of several crypto firms demonstrate, fulsome regulatory oversight is actually a benefit to promising companies because it provides the necessary safety and stability to maintain investor confidence in the market ecosystem. And, as the regulators closest to Main Street businesses and the people who invest in them, the states are prepared to carry a significant share of the regulatory load, much like we have in the crypto space. However, instead of embracing the states as valued partners, all too often Congress and the SEC propose further preemption of state law with little regard to the impact of such actions on investor protection and capital formation.

For the most part, states coordinate and seek consistency. Where beneficial, however, states and their legislatures meet local challenges with local solutions rather than the one-size-fits-all nature of federal regulation. Relatedly, many states provide considerable guidance to small businesses and help them understand their capital-raising options. Consistent with this guidance, the best option for some small businesses may well be registration. Early-stage local businesses are typically less complex than large companies. As a result, the registration process can be much easier.

Many in the securities industry have found it convenient to blame state securities laws for various ills but, upon deeper examination, these laws are seldom the real problem. For example, the SEC's Small Business Capital Formation Advisory Committee recently explored the relative lack of liquidity for secondary trades of securities that were issued under Regulation A. State regulators were once again made the scapegoat for this problem, even though panelists identified a number of more substantive impediments that would not be cured by preempting state law, such as inefficiencies in share transfer recordkeeping and the common practice of issuers demanding a right of first refusal before shares can be resold.

In recent decades, Congress has divided certain regulation between the states and the federal government to achieve efficiencies. This generally has worked well in the context of investment advisers where typically the states register and regulate the small and mid-sized investment advisers and the SEC registers and regulates the large investment advisers.<sup>64</sup> In our view, Congress should build on this concept of complementary regulation by preserving and expanding the responsibility of states with respect to small offerings in our respective states. As a practical matter, small-dollar offerings typically involve local or regional businesses.<sup>65</sup> State regulators are far more likely to handle any enforcement actions for frauds arising out of those offerings. It is not far-fetched to suggest that expanding the role of the states with respect to small offerings would prevent fraud and, relatedly, strengthen local economies.

<sup>64</sup> See [NASAA Letter to Congress](#) Regarding the July 28, 2022, Hearing Questions for the Record (Sept. 14, 2022).

<sup>65</sup> The median distance between a company and the lead investor in a seed round is 94 miles, and the vast majority of angel investments are made with companies in the same region. See SEC, [Office of the Advocate for Small Business Capital Formation Annual Report for Fiscal Year 2022](#) at 30.

### III. Increasing Opportunities for Investors

State regulators interact daily with retail investors. We favor policies to give investors the freedom to choose from a wide range of investment options. However, we believe in full and fair disclosure as a foundational principle that gives investors a realistic chance to be successful in achieving important financial goals. We are very concerned with many of the provisions in the JOBS Act 4.0 because, on whole, they would undermine the disclosures that are currently available in the public markets and make it more likely that investors will suffer harm from the inherent disadvantages in the private markets.

#### A. Investors Are Well-Served by the Public Markets

Efforts to increase investment opportunities for investors should start with policies designed to make the public markets more attractive to companies and their investors. We agree with the sentiments expressed in a Joint Explanatory Statement accompanying the Financial Services and General Government Appropriations Act, 2020: “The Committee believes public markets offer certain valuable benefits to investors that private and quasi-public markets do not provide, including more robust transparency, better pricing efficiency, more accurate valuations, deeper levels of liquidity and lower trading costs, and stronger accountability mechanisms.”<sup>66</sup>

These are extremely important benefits to investors and, by extension, our capital markets. Of course, there are costs associated with being a public company, but our markets are the deepest and most liquid in the world because investors can be confident in their ability to judge the risks of a public offering and assign an appropriate value to a security without having to bear the expense of rigorous due diligence. Investors and their advisors utilize corporate disclosures to gain insight into a wide variety of important issues, such as the company’s financial performance, the strength of its internal controls, and management’s view of challenges facing the company. This contributes to an efficient price discovery mechanism that benefits all investors, including less sophisticated investors who lack awareness or understanding of the disclosures. Unfortunately, however, the advantages of our public markets are easily forgotten because the voices of investors are too often drowned out by those who seek to lessen regulatory requirements despite the proven benefits.

The 2012 JOBS Act is a case in point. While Congress may have hoped for both the private and public markets to thrive as a result of the 2012 JOBS Act, the legislation failed to accomplish the latter. The evidence, as outlined above, shows that the 2012 JOBS Act did not lead to a sustained increase in IPOs. Although it eased the disclosure burdens for companies, it did not

<sup>66</sup> [H. Committee Print of Consolidated Appropriations Act, 2020](#), Comm. on Approp., 116<sup>th</sup> Congress, 2<sup>nd</sup> Session, No. 38-678 (Jan. 2020), at 652. The Committee directed the SEC’s Division of Economic and Risk Analysis to study the performance of Reg A+ and Reg D offerings and within 180 days issue a public report comparing the performance of Reg A+ and Reg D offerings versus all other offerings.

make those companies more attractive to the investors who had to, among other things, assign values to the securities of those companies. Moreover, it expanded the availability of exemptions, which increased the likelihood that companies would stay private longer if not indefinitely.

If, as proposed in the JOBS Act 4.0, Congress continues the trend toward loosening the rules governing the private markets, there is no amount of “easing the disclosure burden” that will entice companies to enter the public market. Ultimately, because companies are able to raise all the capital they need in exempt offerings—through all stages of a company’s typical growth cycle—and there is no meaningful legal requirement to move from the private to public sphere, the typical company will not go public until it is long past its growth stage. The end result of this trend is that retail investors will be left with fewer attractive choices in the public markets.

The better alternative is to focus on strengthening the public markets. This requires a two-fold approach that goes in the opposite direction than the JOBS Act 4.0. First, Congress should scale back Rule 506, which is the primary cause for the explosion of the private markets, and refuse to further expand other exemptions at least until there is far greater data to demonstrate the need for the change and evaluate its deleterious effects on public markets. Second, Congress should establish an appropriate threshold, based on the size of the issuer, its trading activity, or some other metric, at which point a company is required to move from being private to public. In our view, it is time to reinvigorate the bargain that required companies to provide meaningful disclosure in exchange for access to a broad swath of investors.

## **B. Investors Are Not Missing Out on Private Market Opportunities**

Many aspects of the JOBS Act 4.0 rest on the unproven and unlikely assumption that ordinary investors are missing out on great opportunities in the private markets. However, this argument is typically advanced by those who want to expand the pool of eligible investors to sell to, and not the other way around. In reality, retail investors operate in the private markets under extreme disadvantages that minimize their chances for success. Moreover, there is little if any evidence that the typical American household has a pent-up demand for private offerings.

### ***1. The Inherent Disadvantages to Retail Investors in Private Offerings***

To be sure, early-stage companies are an attractive option for certain investors. However, those investors must be equipped to withstand long holding periods, bargain for access to information, and overcome other challenges inherent in private offerings.

As the SEC explained in a 2019 concept release, “Issuers in [Rule 506] offerings are not required to provide any substantive disclosure.”<sup>67</sup> If information is provided at all, it need not be in a fashion that is uniform in content, making comparisons between companies difficult, and the information need not be updated as circumstances change. Voluntary disclosures are prone to greater error and can be influenced by overly optimistic assumptions about future prospects. Further, while Regulation Fair Disclosure<sup>68</sup> requires information about public companies to be distributed in a non-discriminatory fashion, private companies and their insiders are free to provide information to favored investors but not to other investors. In short, investors are left to fend for themselves to obtain unbiased information about the company, and small retail investors are unlikely to have the clout to insist on equitable treatment.

Retail investors enjoy many other benefits of the public markets that ensure a level playing field, and these protections simply do not exist in the private markets. For example, retail investors are assured of getting the best available price on a stock exchange, no matter how small the investment. In the private market, larger or well-known investors can—and often do—receive more favorable terms, and the best deals may only be available to the largest and most influential investors. Prominent venture capital firms, in particular, often negotiate for preferred stock, contractual protection against dilution of their shares in future funding rounds, and representation on the board. Retail investors cannot realistically negotiate for these advantages and therefore may enter into private investments at a disadvantage to other investors in the same company.

Retail investors may also be vulnerable to higher levels of fraud in the private markets. Year after year, state regulators identify unregistered offerings as a top method for conducting fraudulent schemes. Such offerings include ones that are required to be registered and ones that are not required to be registered. Of course, fraud occurs in the public markets, but requirements for strong internal controls, audited financial statements, and other investor protections reduce the likelihood that fraud will remain undiscovered for long. Recent events in the crypto market reveal the damage that can be done to investors in a “Wild West” environment, but state regulators have warned for many years of similar attitudes among unscrupulous actors promoting shares of private companies.

Another benefit of the regulatory framework for public markets comes in the form of important governance and accountability mechanisms that tend to strengthen companies. A tweet by the former President of the New York Stock Exchange, Thomas Farley, sums up how the public markets can prevent meltdowns that occur in poorly managed companies and wipe out billions of dollars of capital:

---

<sup>67</sup> SEC, [Concept Release on Harmonization of Securities Offering Exemptions](#), 84 FED. REG. 30460, 30470 (June 26, 2019).

<sup>68</sup> 17 C.F.R. § 243 (Aug. 2000).

Experiment (sic) of high-growth companies staying private an extra five years was a failure. Uber and WeWork floundered in private markets in last few years and would have benefited from being public. ...Uber. Public markets would not have tolerated lighting a couple billion on fire in futile China effort. Bad behavior by management would have been dealt with quicker. Focus on unit economics would have happened years ago. WeWork. Wave pools. Kindergarten. Questionable accounting. Self-dealing. Poor unit economics. The public market would have squashed this on first earnings call.<sup>69</sup>

Retail investors deserve access to high-quality investment options, and the private market will never give them a realistic chance to compete for those options. Therefore, instead of expanding exemptions in an effort to entice retail investors into an environment where the deck is stacked against them, policymakers should instead look for ways to push more companies with promising growth prospects into the public markets.

## ***2. The Lack of Retail Investor Demand for Private Offerings***

Congress should carefully analyze whether the easing of regulatory safeguards in the JOBS Act 4.0, presumably at the cost of investor protection, would actually result in a countervailing benefit of significant capital formation. Realistically, the expansion of exemptions will yield little additional demand by retail investors for private offerings.

Data from the most recent Survey of Consumer Finances by the Board of Governors of the Federal Reserve System (“SCF”) suggests that companies are unlikely to raise significant capital from retail investors who do not already meet the definition of an accredited investor. According to the SCF, the top ten percent of U.S. households by net worth—a segment of the population that would include most accredited investors—hold 71 percent of the wealth in this country.<sup>70</sup> When one looks beyond that top decile of households, the likelihood of stock ownership falls off dramatically. Even more remote is the likelihood that a household would have a portfolio of securities that is large enough or diversified enough for a financial professional to reasonably recommend the purchase of securities that are exempt from registration. And, if this is the case, it makes little sense for policymakers to open the door for investors to engage directly in the type of activities that, if recommended by a financial professional, would violate the professional’s investor care obligations, including those under the SEC’s Regulation Best Interest.<sup>71</sup>

<sup>69</sup> See @ThomasFarley (Thomas Farley) Twitter (Sept. 22, 2019), available at <https://twitter.com/ThomasFarley/status/1175786943231254531>.

<sup>70</sup> Jesse Bricker, Sarena Goodman, Kevin B. Moore, and Alice Henriques Volz, [Wealth and Income Concentration in the SCF: 1989-2019](#) (Sept. 28, 2020).

<sup>71</sup> See SEC, [Regulation Best Interest, Form CRS and Related Interpretations](#) (last modified Oct. 13, 2022).

Consider the amount of financial assets—which include all bank accounts, certificates of deposit, cash value life insurance, stocks, bonds, and pooled investment funds (including retirement accounts)—held by American households. For the households in the bottom quartile of household net worth, the median value of financial assets held is a mere \$1,380.<sup>72</sup> For the next quartile of households (those between the 25<sup>th</sup> and 50<sup>th</sup> percentiles of net worth), the median value of financial assets held is \$11,220. The next quartile up (between the 50<sup>th</sup> to 75<sup>th</sup> percentiles) is a bit better off, but the median value of financial assets held is still only \$61,000. For three-fourths of American households, then, it is hard to imagine that there would be a significant demand for securities sold in the private markets. Indeed, their investments in high risk, illiquid, unregistered offerings are more likely to be the result of unscrupulous sales tactics rather than sound financial judgment.

Of course, the portion of the population lying just below the current accredited investor thresholds—which would likely include households between the 75<sup>th</sup> and 90<sup>th</sup> percentiles in terms of net worth—is more likely to have the financial wherewithal to invest in private offerings. For these households, the median value of financial assets held is \$301,000.<sup>73</sup> Consider, however, the investment portfolios of these households. For this segment of the population, the median value of retirement accounts is \$192,000, which means that most of these households' financial assets are in retirement accounts.<sup>74</sup> Moreover, barely one in four of these households hold stocks directly,<sup>75</sup> and for those that do, the median value of the holdings is \$30,000.<sup>76</sup>

If a person has \$30,000 to invest directly in stocks, any opportunities available to them in the private markets would be especially risky. It would make little sense to undertake the expense necessary for the level of due diligence that is expected in the private markets, and the investor will be unable to achieve the level of diversification that is common for angel investors and is needed for a reasonable chance of success. Clearly, an investor with this size of investment also would be unable to exert meaningful power to bargain for fulsome disclosure and equitable terms.

As a practical matter, issuers that utilize Rule 506 prefer a small number of large investors rather than a large number of small investors. According to the SEC, Rule 506 offerings include an average of 10 investors and have an average offering size of about \$71 million.<sup>77</sup> Thus, changing the definition of an accredited investor to allow investors of modest means to invest is not likely to be an attractive alternative for promising start-ups, even if those investors are

<sup>72</sup> Board of Governors of the Federal Reserve System, [Survey of Consumer Finances](#), 1989-2019.

<sup>73</sup> *Id.*

<sup>74</sup> *Id.*

<sup>75</sup> *Id.*

<sup>76</sup> *Id.*

<sup>77</sup> SEC Reg A/Reg D Report at 17.

interested. Instead, smaller investors are likely to be left to the sorts of offerings that cannot attract funding from larger, more sophisticated investors.

As described above, offerings conducted under Regulation A and Regulation Crowdfunding suffer from similar dynamics of adverse selection. Given the ease of raising money under Rule 506, promising start-ups should have little difficulty raising money from large, sophisticated investors. Companies conducting offerings under Regulation A or Regulation Crowdfunding tend to be companies that cannot attract those investors, which leaves the highest risk offerings to the smallest of retail investors.

Not surprisingly, existing data shows that investor demand for these offerings is modest, and it is becoming more and more clear that investors are faring poorly in them. As highlighted above, a comprehensive study of Regulation A by the SEC revealed that issuers have sought an average of \$30.1 million in Tier 2 offerings but raised on average only \$15.4 million. In Tier 1, issuers sought an average of \$7.2 million and raised \$5.9 million.<sup>78</sup> Only 45.8 percent of issuers survived at least three years,<sup>79</sup> and the typical issuer continued to realize net losses in the years following the offering.<sup>80</sup> Relatively few Regulation A issuers are listed on a stock exchange, but for those who are, the median annualized buy-and-hold return for their shares was a loss of 47.7 percent. For those listed on the OTC Market, the median loss was 23.9 percent.<sup>81</sup>

Less data is available to determine the amount of investor gains or losses in crowdfunding offerings, but the demand for these offerings is even less than for Regulation A offerings. An SEC study of offerings conducted from May 16, 2016, through December 31, 2018, showed that issuers raised a total of \$107.9 million under Regulation Crowdfunding,<sup>82</sup> and the average offering sought a maximum amount of \$577,385 but raised only \$208,300 (with a median of \$107,367).<sup>83</sup> SEC staff found that crowdfunding securities were characterized by minimal liquidity, and that purchasers of shares had fewer ownership and control rights, such as shareholder voting rights, than was typical for angel- or venture-backed startups. Concern was also expressed that complex payoff structures and other common contractual terms could be difficult for investors to comprehend.<sup>84</sup>

We understand the appeal of measures that appear to give retail investors access to the same types of offerings that are available to the wealthy. It can appear to be unfair to block investors from these deals. In reality, though, there is a wide discrepancy in the quality of offerings in the

<sup>78</sup> *Id.* at 88-89. The SEC raised the offering ceiling in 2020 from \$50 million to \$75 million, but data is not yet available to show the impact of this change. See SEC Harmonization Rule.

<sup>79</sup> SEC Reg A/Reg D Report at 98.

<sup>80</sup> *Id.* at 94.

<sup>81</sup> *Id.* at 99.

<sup>82</sup> SEC Crowdfunding Report at 4.

<sup>83</sup> *Id.* at 3. Despite the modest usage of the exemption, the Commission expanded the allowable offering size to \$5 million in 2020. See SEC Harmonization Rule.

<sup>84</sup> SEC Crowdfunding Report at 21-22.

private markets and all too often retail investors are far more likely to be harmed than helped by exposing them to unregistered offerings. For policymakers troubled by wealth inequality and limited options for building wealth, the continued expansion of exemptions is an unwise solution. The securities laws were originally designed to establish a public market that places retail investors on a level playing field with issuers, and the better approach would be to pursue policies designed to move issuers and investors back onto that field.

#### **IV. NASAA’s Agenda for Reinvigorating the Capital Markets**

NASAA supports an agenda designed to reinvigorate the public markets and improve opportunities for small businesses to thrive. But this will require a turn from the policies that have been pursued in recent decades—policies that were designed to expand the opaque, less regulated private markets. As described more fully in the current NASAA Federal Policy Agenda,<sup>85</sup> we urge Congress to develop legislation that would foster responsible capital formation, protect investors of all ages and backgrounds, and support inclusion and innovation in our capital markets.

##### **A. Promoting Responsible Capital Formation**

First, given the dearth of information that cripples the ability of policymakers to pursue data-driven reforms, we urge Congress to require and fund a comprehensive study on public and private markets led by the SEC’s Division of Economic and Risk Analysis. The study should examine the costs and benefits associated with the monumental shift from public to private markets and, in particular, review the performance of offerings conducted under Regulation A, Regulation D, and Regulation Crowdfunding, as well as the effect of recent changes to the SEC’s definition of an accredited investor.

Second, we call upon Congress to join us in our longstanding efforts to restore oversight and transparency to the private securities markets. Among other such efforts, last Congress, NASAA endorsed S. 4857, the Private Markets Transparency and Accountability Act.<sup>86</sup> This legislation would extend SEC reporting and disclosure requirements to companies that have (i) a valuation of \$700 million (excluding shares held by insiders) or (ii) 5,000 employees and \$5 billion in revenues. Such a change would establish a much-needed mechanism to push large companies into the public sphere and, importantly, could prevent a future company like FTX, WeWork, or

<sup>85</sup> [NASAA Federal Policy Agenda](#) (last updated Jan. 5, 2023).

<sup>86</sup> S. 4857, [Private Markets Transparency and Accountability Act](#), 117<sup>th</sup> Congress, 2<sup>nd</sup> Session. See also [Written Testimony of Michael S. Pleciak, Examining Private Market Exemptions as a Barrier to IPOs and Retail Investment](#) (Sept. 11, 2019).

Theranos from raising billions of dollars from investors unless it discloses fulsome information about its governance and financial condition.<sup>87</sup>

We also support the Promoting Opportunities for Non-Traditional Capital Formation Act,<sup>88</sup> which expands the functions of the SEC's Office of the Advocate for Small Business Capital Formation. Specifically, the legislation would require the SEC's Office of the Advocate for Small Business Capital Formation to (1) provide educational resources and host events to promote capital-raising options for underrepresented small businesses and businesses in rural areas, and (2) meet annually with representatives of state securities commissions to discuss opportunities for collaboration and coordination. Many state securities regulators have existing relationships with organizations that specialize in reaching rural and other hard-to-reach communities, and we believe that increased collaboration will result in better service at both the federal and state levels.

Finally, we call upon Congress to preserve the choice and authority of the states to register and regulate finders. The Unlocking Capital for Small Businesses Act, which was reintroduced in the 117<sup>th</sup> Congress and noticed in discussion draft form for a February 8, 2023, hearing of the HFSC Subcommittee on Capital Markets, would exempt "finders" from registration under federal law and prohibit the states from registering them.<sup>89</sup> Further, it would impose a broker-dealer-lite regulatory regime on private placement brokers. In other words, Congress would be placing additional blindfolds on state and federal regulators. We believe this legislation moves in the wrong direction, and we continue to encourage the SEC and FINRA to collaborate with state securities regulators on changes to the regulatory regime for finders.

## B. Protecting Investors of All Ages and Backgrounds

To prevent investor harm in offerings that are by their nature high-risk, Congress should preserve the choice and authority of the states to register and regulate small offerings, especially ones under \$500,000. These offerings are not typically reviewed by federal authorities, yet the Small Entrepreneurs' Empowerment and Development Act ("SEED Act"), which was reintroduced in the 117<sup>th</sup> Congress and noticed in discussion draft form for a February 8, 2023, hearing of the HFSC Subcommittee on Capital Markets, would take away

<sup>87</sup> In the case of FTX, there is no doubt that stronger disclosure and corporate governance requirements in the private securities markets would have made it easier to spot or prevent the alleged fraud and other misconduct earlier. By way of illustration, under existing law, FTX Trading Ltd. submitted Form D notices to the SEC after raising over \$1.4 billion in capital from dozens of investors. Moreover, in these notices, the corporation only had to disclose basic information regarding it, the offering, the investors, and related fees. Had the law required more timely and fulsome disclosure, regulators and other market watchers may have identified the gaps and weaknesses in FTX's corporate governance earlier. See [NASAA Letter to Congress](#) (Nov. 30, 2022).

<sup>88</sup> H.R. 7977, [Promoting Opportunities for Non-Traditional Capital Formation Act](#), 117<sup>th</sup> Congress, 2<sup>nd</sup> Session.

<sup>89</sup> H.R. \_\_\_\_, [Unlocking Capital for Small Businesses Act of 2023](#), 118<sup>th</sup> Congress, 1<sup>st</sup> Session; S. 3922, [Unlocking Capital for Small Businesses Act of 2022](#), 117<sup>th</sup> Congress, 2<sup>nd</sup> Session.

existing state authority to protect investors and businesses.<sup>90</sup> The likely result is fundraising mistakes by well-meaning companies and fraud perpetrated against investors and entrepreneurs.

Similarly, Congress should prevent investor harm by preserving the choice and authority of states to require notices to the states of certain securities transactions. The Facilitating Main Street Offerings Act<sup>91</sup> and the Improving Crowdfunding Opportunities Act,<sup>92</sup> which were introduced in the 117<sup>th</sup> Congress, would prohibit state governments from using an important tool – regulatory notices called notice filings – to keep track of capital-raising efforts in their states and prevent harm to investors. The Improving Crowdfunding Opportunities Act was noticed in discussion draft form for a February 8, 2023, hearing of the HFSC Subcommittee on Capital Markets. Though the Facilitating Main Street Offerings Act was not noticed for the February 8 hearing, similar, more expansive legislation was noticed. Specifically, lawmakers noticed a bill in discussion draft form that would amend the Securities Act to exempt off-exchange secondary trading from state regulation where such trading is with respect to securities of an issuer that makes publicly available certain information required under federal securities laws.<sup>93</sup> If these or similar types of bills were to become law, dozens of state governments would no longer have the choice of using certain tools for investor protection, including notice filings.<sup>94</sup>

To protect investors from bad actors and bolster oversight and accountability of Wall Street, Congress should strengthen the SEC’s ability to crack down on violations of securities laws. Under existing law, in some cases involving fraud with substantial losses, the SEC can only penalize individual violators a maximum of \$189,693 and institutions \$916,850.<sup>95</sup> In other cases, the SEC may calculate penalties to equal the gross amount of ill-gotten gain but only if the matter goes to federal court, not when the SEC handles a case administratively. We urge Congress to update and enhance the SEC’s civil penalties statute by increasing the statutory limits on civil monetary penalties, directly linking the size of these penalties to the scope of harm and associated investor losses, and substantially raising the financial stakes for repeat securities law violators.

Further, to assist state regulators in their efforts to protect investors, we urge Congress to require the federal financial regulators to establish a bad actors database and allow state and

<sup>90</sup> H.R. \_\_, [SEED Act of 2023](#), 118<sup>th</sup> Congress, 1<sup>st</sup> Session; H.R. 5458, [SEED Act of 2021](#), 117<sup>th</sup> Congress, 1<sup>st</sup> Session.

<sup>91</sup> S. 3966, [Facilitating Main Street Offerings Act](#), 117<sup>th</sup> Congress, 2<sup>nd</sup> Session.

<sup>92</sup> H.R. \_\_, [the Improving Crowdfunding Opportunities Act](#), 118<sup>th</sup> Congress, 1<sup>st</sup> Session; S. 3967, [Improving Crowdfunding Opportunities Act](#), 117<sup>th</sup> Congress, 2<sup>nd</sup> Session.

<sup>93</sup> H.R. \_\_, [To amend the Securities Act of 1933 to exempt off-exchange secondary trading from State regulation where such trading is with respect to securities of an issuer that makes publicly available certain current information, and for other purposes](#), 118<sup>th</sup> Congress, 1<sup>st</sup> Session.

<sup>94</sup> See [NASAA UFT Submission System – State Participation](#) (as of July 18, 2022).

<sup>95</sup> See SEC, [Inflation Adjustments to the Civil Monetary Penalties Administered by the Securities and Exchange Commission](#) (as of Jan. 15, 2022).

local governments to participate in it. The Tracking Bad Actors Act,<sup>96</sup> which was introduced in the 117<sup>th</sup> Congress, would require the establishment of such a database.

### C. Supporting Inclusion and Innovation in Our Capital Markets

The emergence of digital assets has brought innovation to our capital markets. It also serves as a cautionary tale as we have witnessed the implosion of what were touted as safe and promising investment opportunities. This underscores the importance of preserving the securities regulatory framework as Congress considers legislation relating to digital assets, and we urge Congress to resist calls to shift oversight away from the SEC or otherwise weaken the fulsome protections that investors deserve. We also note that state securities regulators, as the local “cops on the beat” who are often the first to observe troubling patterns or behaviors, should have a seat at the table in any digital asset working groups or other multi-agency efforts.

To further enhance federal and state collaboration in our mutual goals of investor protection, Congress should modernize the Financial Literacy Education Commission (“FLEC”).<sup>97</sup> Two decades after the creation of the FLEC, much has changed in the way people communicate, save, and invest, and Congress should consider ways to update and strengthen investor education. In conjunction with this effort, Congress should include a representative of state securities regulators as a member of FLEC. Current members include numerous federal government agencies and offices such as the SEC, the Federal Trade Commission, the Department of Education, and the Department of Defense, but there is no representation from state governments.

An important aspect of any agency’s investor protection mission is to educate and inform investors. State regulators work hard to reach investors, devoting time and energy to speak at senior centers, teacher conferences, and other events. They also try to take advantage of social media to spread the word about current scams and other dangers. In this digital age, though, it is challenging for state and federal regulators to compete with questionable “advice” offered through forums like WallStreetBets or the hype of the latest non-fungible token. We urge Congress to examine the resources that are devoted to investor education and pursue policies designed to bolster those efforts, including providing more resources to the SEC so that it can communicate its important message effectively.

Finally, as discussed above, the definition of an accredited investor is a critical component for protecting investors and restoring balance between our public and private markets. We therefore call upon Congress to reverse the deleterious impact of four decades of inflation on the existing net worth and income standards. To achieve this, Congress should raise the current income and net worth thresholds for natural persons and index those thresholds to inflation. Furthermore, just as a person’s primary residence does not count towards the \$1

<sup>96</sup> S. 3716, [Tracking Bad Actors Act of 2022](#), 117<sup>th</sup> Congress, 2<sup>nd</sup> Session.

<sup>97</sup> 20 U.S.C. §§ 9701-9709.

million net asset threshold required for accredited investor status, Congress should add an exclusion for the value of any defined benefit or defined contribution tax-deferred retirement accounts, as well as the value of agricultural land and machinery held for production. And, while we agree that sophistication of the investor should be considered a central aspect of the definition, metrics to measure sophistication should include demonstrable investment experience. Importantly, as this report makes clear, no amount of sophistication can substitute for meaningful access to information and the ability to withstand losses.

**Appendix**

**NASAA Positions as of February 2023 Regarding the Proposals in the Draft JOBS Act 4.0 Published in April 2022<sup>98</sup>**

**Section 101: Middle Market IPO Cost Underwriting Act**

<p><b>117<sup>th</sup> Congress</b> + <a href="#">S. 3980</a> (Lummis)</p>	<p>+ Directs the SEC, in consultation with FINRA, to study the costs associated with underwriting IPOs and Regulation A, Tier 2 offerings for small- and medium-sized companies (less than \$700M initial public float) + Directs the SEC to issue a report to Congress with findings and recommendations</p>	<p><b>QUALIFIED SUPPORT.</b> This work should be done as part of a holistic study of the U.S. capital markets. Such a study would help the policymaking community make data-driven decisions on how best to restore the primacy of public markets in the United States and protect and empower investors.</p>
<p><b>115<sup>th</sup> Congress</b> + <a href="#">S. 488</a> (Toomey) + <a href="#">H.R. 6324</a> (Himes)</p>		

<sup>98</sup> The far-left column of the chart lists present and prior versions of the legislation. NASAA included the bill even if it is not an exact match for the bill that is in the discussion draft of the JOBS Act 4.0. In many cases, the text of the bill has changed since its initial introduction. We also included the last name of the introducing lawmaker. Use the hyperlinks to the legislation to look up additional sponsors. In the center column, NASAA summarized the key provisions of the version of the bill that is in the discussion draft of the JOBS Act 4.0. In the far-right column of the chart, we provided a basic, high-level explanation of NASAA's position.

**Section 102: Emerging Growth Company Extension Act**

<p>117<sup>th</sup> Congress + <a href="#">H.R. 3448</a> (Steil)</p> <p>116<sup>th</sup> Congress + <a href="#">H.R. 4918</a> (Steil)</p> <p>115<sup>th</sup> Congress + <a href="#">H.R. 6130</a> (Rothfus)</p>	<p>+ Extends the maximum period that EGCs (<i>i.e.</i>, newly public companies) have to undertake certain disclosure and other requirements from five to 10 years</p> <p>+ Directs the SEC to issue an interim final rule within 180 days to make the change yet prohibits the SEC when doing so from soliciting feedback relevant to the change</p>	<p><b>OPPOSE.</b> Extending EGC status from five years to 10 years, thereby allowing a company to scale its disclosures and abstain from SOX internal control audits for a full decade, suggests that these disclosures and internal controls are of negligible value to investors. However, a lesson of the 2012 JOBS Act is that the reduction of the disclosure “burden” for EGCs did not lead to an increase in IPOs. Rather, the reduced disclosure made it more difficult for investors to price the securities. Ultimately, whatever companies saved in accounting and related expenses, they more than lost because their shares were underpriced by the market in IPOs and were more volatile post-IPO. If Congress proceeds further down the path of eroding the disclosure requirements for public companies, the likely outcome is a less attractive marketplace for Americans to invest. Instead, Congress should direct the SEC to study the supply side of the equation (<i>i.e.</i>, what can be done responsibly, particularly through technology, to lower the cost of going public) and the demand side of the equation (<i>i.e.</i>, what do investors want). This work should be done as part of a holistic study of the U.S. capital markets. This study would help the policymaking community make data-driven decisions on how best to restore the primacy of public markets in the United States and protect and empower investors.</p>
--	--	--

## NASAA REPORT AND RECOMMENDATIONS FOR REINVIGORATING OUR CAPITAL MARKETS

**Section 103: Dodd-Frank Material Disclosure Improvement Act**

<p>117<sup>th</sup> Congress + <a href="#">S. 3923</a> (Cramer) + <a href="#">H.R. 3276</a> (Huizenga)</p> <p>115<sup>th</sup> Congress + <a href="#">H.R. 10</a> (Hensarling) + <a href="#">H.R. 4519</a> (Huizenga) + <a href="#">H.R. 4289</a> (Mooney) + <a href="#">H.R. 4248</a> (Huizenga)</p> <p>114<sup>th</sup> Congress: + <a href="#">H.R. 5983</a> (Hensarling)</p>	<p>+ Repeals the conflict minerals, mine safety, resource extraction, and pay ratio provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act and the rules promulgated thereunder</p> <p>+ Prohibits the SEC from issuing rules that are substantially similar to the repealed rules</p>	<p><b>UNDER REVIEW.</b> NASAA generally supports efforts to reform federal securities laws to promote greater transparency and comparability of information that is material to investors. We would oppose this legislation to the extent it interferes with the disclosure of material information to investors. As an alternative, Congress could give the SEC the authority to repeal these currently-mandated rules if the Commission finds, through investor testing, that the information is not material.</p>
--	---	--

**Section 104: Reporting Requirements Reduction Act of 2022**

<p>117<sup>th</sup> Congress + <a href="#">S. 3919</a> (Tillis)</p>	<p>+ Allows public companies to disclose important financial and other information regarding the company on a semiannual basis rather than on a quarterly basis</p>	<p><b>OPPOSE.</b> <a href="#">Survey data</a> demonstrates that investors overwhelmingly oppose this idea. Current financial information is necessary to support price discovery in our markets, and trust in the markets in large part stems from the promise that our public companies will make certain information about themselves available to the investing public either promptly or periodically. Moving from quarterly to semi-annual reporting would weaken the markets because it would lead to greater price dislocation and volatility, which would stifle capital formation. Moreover, the COVID-19 pandemic was a helpful reminder of the important role that quarterly disclosure can serve in unexpected, evolving situations. For these and other reasons, it would be ill-advised to reduce the frequency of corporate reporting, but we generally are supportive of efforts to understand how technology could be used responsibly to lower the costs of quarterly reporting.</p>
---	---	--

Section 105: Restoring Shareholder Transparency Act		
<p>117<sup>th</sup> Congress + <a href="#">S. 3945</a> (Hagerty)</p> <p>115<sup>th</sup> Congress: + <a href="#">H.R. 10</a> (Hensarling)</p>	<p>+ Excludes all but the wealthiest shareholders from participating fully in the governance of public companies by imposing a requirement that a shareholder must hold at least 1% of the market value of the company's securities to submit a proposal for corporate reform</p> <p>+ Permits public companies to opt-out of SEC rules governing shareholder proposals</p> <p>+ Clarifies the applicability of certain SEC rules to investment professionals who provide advice to clients on how to vote on shareholder proposals</p>	<p><b>OPPOSE.</b> Shareholders are the owners of companies. Policymakers should strengthen, not weaken, their right to raise issues with respect to the governance of the company. This section would allow only the largest shareholders to exercise that right. We oppose proposals such as this one that would reduce the costs of corporate governance through deregulation and exclusion. However, we generally support efforts to understand how technology could be used responsibly to lower the costs of corporate governance, increase participation in corporate governance, increase participation in our markets by people of all ages and backgrounds, and strengthen the rights of shareholders.</p>
Section 106: Increasing Access to Adviser Information Act		
<p>117<sup>th</sup> Congress + <a href="#">S. 3965</a> (Moran)</p>	<p>+ Allows larger providers of investment research with clients in Europe to avoid registration with the SEC as an investment adviser</p>	<p><b>OPPOSE.</b> In a <a href="#">February 2022 SEC staff report</a> regarding investment research, SEC staff observed that some larger providers of investment research with clients in Europe that were registered previously as broker-dealers have registered as investment advisers to ensure their compliance with U.S. and E.U. laws. Investment research providers with cross-Atlantic businesses should act promptly to ensure they are in compliance with U.S. and E.U. laws.</p>

**Section 107: The Main Street Growth Act**

<p><b>117<sup>th</sup> Congress</b>                  + <a href="#">S. 3097</a> (Kennedy)                  + <a href="#">H.R. 5795</a> (Emmer)</p> <p><b>116<sup>th</sup> Congress</b>                  + <a href="#">S. 2306</a> (Kennedy)                  + <a href="#">H.R. 2899</a> (Emmer)</p> <p><b>115<sup>th</sup> Congress</b>                  + <a href="#">S. 488</a> (Toomey)                  + <a href="#">S. 3723</a> (Kennedy)                  + <a href="#">H.R. 5877</a> (Emmer)</p> <p><b>114<sup>th</sup> Congress</b>                  + <a href="#">H.R. 5983</a>                  (Hensarling)                  + <a href="#">H.R. 4638</a> (Garrett)</p>	<p>+ Establishes a regulatory framework for registration with the SEC of national venture securities exchanges dedicated to the trading of “venture securities”</p> <p>+ Requires the SEC to promulgate regulations to ensure the issuers of and investors in venture securities are provided disclosures sufficient to understand venture securities-trading</p>	<p><b>OPPOSE.</b> Venture exchanges have been <u>tried before without success</u>. Nothing in current law prohibits them, and a regulatory solution is unlikely to solve what is a market-based problem. In short, investors are not very interested in securities that are listed on an exchange with weak listing standards. In addition, institutional investors tend to avoid investing significant sums in small companies because the price can move dramatically against them when they try to exit the position. Even without a venture exchange, venture capital investments have flourished, and Congress should direct the SEC to study the many existing paths available for venture capital investments and make recommendations to Congress on ways to offer additional support to this part of the market. This work should be part of a holistic study on the U.S. capital markets. Such a study would help the policymaking community make data-driven decisions on how best to restore the primacy of public markets in the United States and protect and empower investors.</p>
--	---	--

**Section 108: The Intelligent Tick Study Act**

<p><b>117<sup>th</sup> Congress</b> + <a href="#">S. 3947</a> (Kennedy)</p>	<p>+ Directs the SEC to study and submit to Congress a report that examines the transition to trading and quoting securities in increments other than \$0.01; the impact that the change in increment has had on liquidity and market quality for small, middle, and large capitalization company securities; and whether there is sufficient economic incentive to support trading operations in increments other than \$0.01 + Permits the SEC to conduct rulemaking to designate a minimum increment for EGC securities that is greater than \$0.01 but not more than \$0.25</p>	<p><b>UNDER REVIEW.</b> Smaller tick sizes in liquid securities may yield better execution quality, so a study to determine the impact of potential changes to tick sizes should include a review of sub-penny quotes for highly liquid securities as well as ticks in excess of a penny for less liquid securities. Moreover, consistent with our view that Congress must place the interests of investors front-and-center, we urge lawmakers to consider alternative options for stimulating more research, particularly research on small cap companies. We are pleased to see that the SEC has issued a proposal to address illiquidity in certain securities due to tick sizes.</p>
---	---	---

**Section 201: Expanding Access to Capital for Rural Job Creators Act**

<p><b>118<sup>th</sup> Congress</b> + <a href="#">H.R. 298</a> (Mooney)</p> <p><b>117<sup>th</sup> Congress</b> + <a href="#">S. 3503</a> (Kennedy) + <a href="#">H.R. 5128</a> (Axne)</p> <p><b>116<sup>th</sup> Congress</b> + <a href="#">S. 566</a> (Jones) + <a href="#">H.R. 2409</a> (Axne)</p> <p><b>115<sup>th</sup> Congress</b> + <a href="#">S. 488</a> (Toomey) + <a href="#">S. 2953</a> (Jones) + <a href="#">H.R. 4281</a> (Kihuen)</p>	<p>+ Requires the SEC Advocate for Small Business Capital Formation to identify any unique challenges that rural-area small businesses have with securing access to capital + Requires the advocate to also report annually on the most serious issues encountered by rural-area small businesses and their investors</p>	<p><b>SUPPORT.</b> While NASAA supports the text of this proposal as-is, we urge Congress to incentivize this SEC office to collaborate and coordinate better with NASAA and its members. Involving us in this important work would yield better results for Congress and the rural-area small businesses and investors that we are all trying to support. In addition, Congress should identify opportunities for improvement in the coordination between the Small Business Administration and the SEC on outreach to rural communities.</p>
---	---	--

Section 202: Expanding American Entrepreneurship Act		
<p><b>117<sup>th</sup> Congress</b> + <a href="#">S. 3976</a> (Moran)</p>	<p>+ Expands the universe of qualifying venture capital funds that can exist without having to register with the SEC by increasing the maximum invested capital level and the number of investors</p> <p>+ Increases the maximum invested capital level from \$10M to \$50M</p> <p>+ Increases the number of permitted beneficial investors from 250 to 500</p>	<p><b>OPPOSE.</b> Past changes to the securities laws governing investment funds have paved the way for a surge in private capital. The explosive growth of venture capital funds has created a seemingly bottomless source of capital for private companies, allowing them to substantially delay going public or remain private indefinitely. Rather than passing more deregulatory legislation that probably will expand our private markets again, Congress should direct the SEC to conduct a holistic study on the U.S. capital markets. This study would help the policymaking community make data-driven decisions on how best to restore the primacy of public markets in the United States and protect and empower investors.</p>
Section 203: Developing and Empowering Our Aspiring Leaders Act of 2022		
<p><b>118<sup>th</sup> Congress</b> + <a href="#">H.R. _____</a></p> <p><b>117<sup>th</sup> Congress</b> + <a href="#">S. 3914</a> (Rounds) + <a href="#">H.R. 4227</a> (Hollingsworth)</p> <p><b>116<sup>th</sup> Congress</b> + <a href="#">H.R. 8603</a> (Hollingsworth)</p> <p><b>115<sup>th</sup> Congress</b> + <a href="#">S. 488</a> (Toomey) + <a href="#">S. 3576</a> (Rounds) + <a href="#">H.R. 6177</a> (Hollingsworth)</p>	<p>+ Requires the SEC to expand the definition of qualifying investment for venture capital funds to include broader equity securities and venture capital investments in other funds</p> <p>+ Allows venture capital funds to make these qualifying investments without having to register with the SEC as a registered investment adviser</p>	<p><b>OPPOSE.</b> Past changes to the securities laws governing investment funds have paved the way for a surge in private capital. The explosive growth of venture capital funds has created a seemingly bottomless source of capital for private companies, allowing them to substantially delay going public or remain private indefinitely. Rather than passing more deregulatory legislation that probably will expand our private markets again, Congress should direct the SEC to conduct holistic study on the U.S. capital markets. This study would help the policymaking community make data-driven decisions on how best to restore the primacy of public markets in the United States and protect and empower investors.</p>

**Section 204: Small Entrepreneurs' Empowerment and Development Act of 2022**

<p><b>118<sup>th</sup> Congress</b> + <a href="#">H.R. _____</a> (McHenry)</p> <p><b>117<sup>th</sup> Congress</b> + <a href="#">S. 3939</a> (T. Scott) + <a href="#">H.R. 5458</a> (McHenry)</p> <p><b>115<sup>th</sup> Congress</b> + <a href="#">H.R. 10</a> (Hensarling) + <a href="#">H.R. 2201</a> (Emmer)</p> <p><b>114<sup>th</sup> Congress</b> + <a href="#">H.R. 5983</a> (Hensarling) + <a href="#">H.R. 2357</a> (Wagner) + <a href="#">H.R. 4850</a> (Emmer)</p>	<p>+ Enacts a micro-offering safe harbor that would exempt a sale of securities if the total amount of securities sold by the issuer during the preceding 12-month period sale does not exceed \$500,000</p> <p>+ Preempts state registration and notice filing authority for these securities</p>	<p><b>OPPOSE.</b> We oppose the provisions of this legislation that weaken state investor protection laws. States should be recognized as the primary regulators of these offerings that tend to be localized economic development efforts. State securities regulators regularly witness firsthand the value that comes from having small businesses engage directly with local regulators regarding small-dollar offerings. This engagement helps entrepreneurs better understand their options for raising capital, avoid missteps, and deter fraud and other misconduct that can harm legitimate businesses and investors alike. Importantly, state regulation also facilitates investor access to information necessary to make informed investment decisions, thus enhancing the fairness and efficiency of our capital markets. We cannot protect investors if we lack a line of sight into companies selling these securities.</p> <p>In addition, we believe this legislation is unnecessary. There are more avenues than ever to raise capital, especially for an offering of \$500,000 or less. Before expanding those options, Congress should direct the SEC to conduct a holistic study on the U.S. capital markets. This study would help the policymaking community make data-driven decisions on how best to restore the primacy of public markets in the United States and protect and empower investors.</p>
--	--	---

**Section 205: Unlocking Capital for Small Businesses Act of 2022**

<p><b>118<sup>th</sup> Congress</b> + <a href="#">H.R. _____</a></p> <p><b>117<sup>th</sup> Congress</b> + <a href="#">S. 3922</a> (Kramer) + <a href="#">H.R. 8998</a> (Budd)</p> <p><b>116<sup>th</sup> Congress</b> + <a href="#">H.R. 3768</a> (Budd)</p> <p><b>115<sup>th</sup> Congress</b> + <a href="#">H.R. 6127</a> (Budd)</p>	<ul style="list-style-type: none"> <li>+ Exempts “finders” from registration under federal law and prohibits state registration</li> <li>+ Permits securities brokers to be treated as a “finder” in a given calendar year if they are paid less than \$500K; conduct fewer than 16 unrelated transactions; or do deals valued at less than \$30M</li> <li>+ Imposes a broker-dealer-light regulatory regime on private placement brokers</li> <li>+ Defines “private placement broker” as one that introduces securities issuers and securities buyers engaged in private deals, and is not a finder</li> </ul>	<p><b>OPPOSE.</b> We oppose bills that would prohibit or restrict state regulatory oversight of “finders” and “private placement brokers.” Prior to conducting business in our state, most securities brokers must go through a licensing and registration process. It is an essential opportunity for regulators to learn about these businesses and to have some confidence that the professionals understand the basics of state securities laws before they solicit investors. State securities regulators cannot protect investors or otherwise support responsible capital formation if we lack a line of sight into who is promoting securities in our state.</p> <p>Rather than legislating in this area, we urge Congress to call on the SEC and FINRA to work together and to work with state securities regulators on appropriate changes to the existing regulatory framework applicable to these market participants. As NASAA has stated in past letters to Congress and the SEC, we believe the more effective path forward is to have the regulators discuss and make appropriate improvements.</p>
--	--	---

Section 206: Small Business Mergers, Acquisitions, Sales, and Brokerage Simplification Act of 2021		
<p><b>117<sup>th</sup> Congress</b> + <a href="#">S. 3391</a> (Kennedy) + <a href="#">H.R. 935</a> (Huizenga)</p>	<p>+ Provides an exemption from registration with the SEC for a subset of brokers called merger and acquisition brokers (“M&amp;A brokers”)</p>	<p>This legislation became federal law during the 117th Congress. NASAA supported the legislation.</p>
<p><b>116<sup>th</sup> Congress</b> + <a href="#">H.R. 609</a> (Huizenga)</p>	<p>+ Restricts the universe of brokers who can qualify for this exemption to ones that, among other</p>	
<p><b>115<sup>th</sup> Congress</b> + <a href="#">S. 488</a> (Toomey) + <a href="#">S. 3518</a> (Peters) + <a href="#">H.R. 10</a> (Hensarling) + <a href="#">H.R. 477</a> (Huizenga)</p>	<p>requirements, do not facilitate securities transactions with groups of buyers formed with the assistance of the M&amp;A broker</p>	
<p><b>114<sup>th</sup> Congress</b> + <a href="#">S. 1010</a> (Manchin) + <a href="#">H.R. 686</a> (Huizenga)</p>		

NASAA REPORT AND RECOMMENDATIONS FOR REINVIGORATING OUR CAPITAL MARKETS

**Section 301: Small Business Audit Correction Act**

<p><b>117<sup>th</sup> Congress</b> + <a href="#">S. 4292</a> (Cotton)</p> <p><b>116<sup>th</sup> Congress</b> + <a href="#">S. 2724</a> (Cotton) + <a href="#">H.R. 8983</a> (Hill)</p> <p><b>115<sup>th</sup> Congress</b> + <a href="#">S. 3004</a> (Cotton) + <a href="#">H.R. 6021</a> (Hill)</p>	<p>+ Exempts privately held, non-custodial brokerage firms in good standing from a requirement to have a Public Company Accounting Oversight Board (PCAOB)-registered firm conduct their annual audit</p>	<p><b>OPPOSE.</b> We oppose this legislation because it exposes investors and other market participants to possible fraud as a result of lax and inferior audit practices. Broker-dealers are important financial intermediaries and should be held to high standards, including audits by PCAOB-registered firms who must meet a widely recognized and uniform standard of expertise. Also, in our experience, the brokers that would be willing to cut costs in this way probably will cut costs in other ways—all to the detriment of their customers. For example, they probably are willing to cut corners on other books and records.</p>
--	---	---

**Section 302: Access to Small Business Investor Capital Act**

<p><b>117<sup>th</sup> Congress</b> + <a href="#">S. 3961</a> (Daines) + <a href="#">H.R. 5598</a> (Sherman)</p> <p><b>116<sup>th</sup> Congress</b> + <a href="#">H.R. 7375</a> (Sherman)</p>	<p>+ Allows registered investment companies, such as mutual funds, to exclude specified fees and expenses from the fund's fee table disclosure for investors and provide the information in a footnote instead</p> <p>+ Such fees are the ones the fund incurs indirectly when purchasing shares of a business development company, which is a type of fund that invests in financially distressed or developing firms</p>	<p><b>OPPOSE.</b> We oppose this legislation because it obscures the "bottom-line" costs of investing in certain funds. The "bottom line" or "all-in" costs of investing in a fund are important to investors and fund disclosures should give investors that information in a form that is simple to digest.</p>
--	--	---

Section 303: Gig Worker Equity Compensation Act		
<p><b>118<sup>th</sup> Congress</b> + <a href="#">H.R. _____</a> (McHenry)</p> <p><b>117<sup>th</sup> Congress</b> + <a href="#">S. 3931</a> (Lummis) + <a href="#">H.R. 2990</a> (McHenry)</p> <p><b>116<sup>th</sup> Congress</b> + <a href="#">H.R. 8280</a> (McHenry) + <a href="#">H.R. 6254</a> (McHenry)</p>	<p>+ Requires the SEC to extend exemptions for securities that apply to employees of the issuer to individuals (other than employees) providing goods for sale, labor, or services for remuneration to an issuer, or to customers of an issuer</p>	<p><b>OPPOSE.</b> Non-cash equity incentives have a reputation as “<a href="#">golden handcuffs</a>” because a substantial part of an employee’s compensation may be tied up in these equity incentives. These Rule 701 offerings are illiquid and subject to valuation risk given the lack of public financial disclosure by non-reporting issuers. The shares awarded to employees may have inferior rights to those issued to founders or institutional investors, and the employee’s shares may suffer substantial dilution as a result of subsequent offerings. Instead of addressing these concerns, this legislation would allow companies to extend equity awards to gig workers or customers, who are even less likely than employees to have bargaining power and insights into the financial prospects of the company. This increases the risk that companies will take unfair advantage of them. It could also facilitate the use of stock compensation to incentivize promoters to improperly tout and “pump” the price of the issuer’s securities.</p>

**Section 304: Increasing Investor Opportunities Act**

<p><b>118<sup>th</sup> Congress</b> + <a href="#">H.R. _____</a> (Wagner)</p>	<p>+ In effect, expands the participation of closed-end funds in private funds</p>	<p><b>OPPOSE.</b> Past changes to the securities laws governing investment funds have paved the way for a surge in private capital. Our private markets provide less disclosure, less liquidity, and weak price discovery. Rather than passing more legislation that probably will expand these markets, Congress should direct the SEC to conduct a holistic study on the U.S. capital markets. This study would help the policymaking community make data-driven decisions on how best to restore the primacy of public markets in the United States and protect and empower investors.</p>
<p><b>117<sup>th</sup> Congress</b> + <a href="#">S. 3948</a> (Daines) + <a href="#">H.R. 4262</a> (Gonzalez)</p>	<p>+ Prohibits the SEC from restricting the investments of closed-end funds in private funds solely or primarily because of the private funds' status as private funds</p>	
<p><b>116<sup>th</sup> Congress</b> + <a href="#">H.R. 8786</a> (Gonzalez)</p>	<p>+ Prohibits exchanges from prohibiting the listing or trading of a closed-end fund's securities solely or primarily by reason of the amount of the company's investment in private funds</p>	

NASAA REPORT AND RECOMMENDATIONS FOR REINVIGORATING OUR CAPITAL MARKETS

**Section 305: Improving Crowdfunding Opportunities Act**

<p><b>118<sup>th</sup> Congress</b> + <a href="#">H.R. _____</a> (McHenry)</p> <p><b>117<sup>th</sup> Congress</b> + <a href="#">S. 3967</a> (Moran) + <a href="#">H.R. 9478</a> (McHenry)</p>	<ul style="list-style-type: none"> <li>+ Prohibits state securities regulators from requiring securities issuers to report information to the states regarding trades of their securities made through funding portals</li> <li>+ Reverses an SEC interpretation of Regulation CF that treats crowdfunding portals as issuers for liability purposes by stating portals will not be treated as issuers unless they knowingly lie or mislead investors or otherwise engage in a fraud upon them</li> <li>+ Excludes funding portals from the recordkeeping and reporting requirements of the Bank Secrecy Act</li> <li>+ Explicitly permits impersonal investment advice and recommendations by funding portals that does not purport to meet the objectives or needs of a specific individual or account</li> </ul>	<p><b>OPPOSE.</b> We oppose efforts to weaken state investor protection laws. Our primary job is to protect investors and promote responsible capital formation in our states. While the SEC similarly protects investors and promotes capital formation, it does not take the kind of grassroots approach that is typical of state agencies. Given the SEC’s track record on crowdfunding rulemaking and enforcement, Congress should assume the SEC will not (1) take enforcement actions in crowdfunding-related cases that involve losses under \$1 million and (2) support local, small startups in all 50 states. Therefore, it would be unwise to preempt the states, who serve as the de facto primary regulator in these offerings. Furthermore, the restriction of portal liability will likely lead to more aggressive practices by funding portals and ultimately damage the credibility of offerings made under Reg CF.</p>
--	---	--

Section 306: Equal Opportunity for All Investors Act		
<p><b>118<sup>th</sup> Congress</b> + <a href="#">H.R. _____</a> (McHenry)</p> <p><b>117<sup>th</sup> Congress</b> + <a href="#">S. 3921</a> (Tillis) + <a href="#">H.R. 4776</a> (McHenry) + <a href="#">H.R. 4708</a> (Huizenga)</p>	<p>+ Expands the universe of persons who would qualify for accredited investor status</p> <p>+ Directs the SEC to establish or approve an exam and permits an individual to certify she is an accredited investor by passing an exam approved by the SEC, a state securities regulator, or an SRO</p> <p>+ Directs the SEC to treat (1) persons with at least \$500K worth of investments and (2) persons investing no more during a 12-month period than either (a) 10% of their total investments; (b) 10% of their annual income; or (c) 10% of their net worth excluding one's home, as accredited investors</p> <p>+ Defines terms for these purposes, including digital assets</p> <p>+ Permits issuers to rely on self-certifications absent reckless disregard or knowledge of contrary information</p>	<p><b>UNDER REVIEW.</b> NASAA has significant concerns regarding this legislation. The accredited investor definition plays a central role in our markets. Private issuers that limit their sales to accredited investors can raise unlimited money in a private offering without having to register those securities or otherwise comply with the full range of regulations designed to promote market transparency and integrity, the efficient allocation of capital, and the protection of investors. Self-certification can be abused by unscrupulous promoters who convince investors to make such representations to place them into high-cost, high-risk, illiquid, or fraudulent offerings.</p> <p>Congress should direct the SEC to study, in consultation with NASAA, the anticipated consequences for the U.S. capital markets of this legislation. A holistic study would help the policymaking community make data-driven decisions.</p> <p>If it were to act earlier, Congress should raise the current income and net worth thresholds for natural persons and index those thresholds to inflation. Just as a person's primary residence does not count towards the \$1 million net asset threshold required for accredited investor status, Congress should add an exclusion for the value of any defined benefit or defined contribution tax-deferred retirement accounts, as well as the value of agricultural land and machinery held for production. And, while we agree that sophistication of the investor should be considered a central</p>

## NASAA REPORT AND RECOMMENDATIONS FOR REINVIGORATING OUR CAPITAL MARKETS

		aspect of the definition, metrics to measure sophistication should include demonstrable investment experience, and no amount of sophistication can substitute for meaningful access to information and the ability to withstand losses.
<b>Section 307: Facilitating Main Street Offerings Act</b>		
<p>118<sup>th</sup> Congress + <a href="#">H.R. _____</a></p> <p>117<sup>th</sup> Congress + <a href="#">S. 3966</a> (Moran)</p>	<p>+ Undermines responsible capital formation and investor protection by preempting state securities regulation of secondary trading of Regulation A securities issued in Tier 2 offerings</p>	<p><b>OPPOSE.</b> We strongly oppose efforts to weaken state investor protection laws, including this legislation and similar legislation that the HFSC noticed in discussion draft form in connection with a February 8, 2023, hearing of the Subcommittee on Capital Markets. See <a href="#">H.R. _____</a>, to amend the Securities Act of 1933 to exempt off-exchange secondary trading from State regulation. The federal government’s previous decision to preempt the states from primary offerings conducted under Regulation A, Tier 2 did not improve either the quality or marketability of these offerings. In our experience, rather than suffering from an undue regulatory burden, this market suffers much more from a lack of demand because investors want to avoid high costs, high information asymmetries, and high investment minimums. Similarly, the secondary trading of these securities is hindered by a variety of factors such as inefficiencies in share transfer recordkeeping and the fact that the issuer usually has a right of first refusal. There is very little evidence that state regulation is a primary cause of illiquidity in these offerings, and preemption will not solve the problem. Instead, it will harm investors by removing state securities regulators’ line of sight into the trading of these securities.</p>

Section 308: Retirement Savings Modernization Act		
<p>117<sup>th</sup> Congress                      + <a href="#">S. 4973</a> (Toomey)                      + <a href="#">H.R. 9066</a> (Meijer)</p>	<p>+ Provides that the selection or maintenance of a multi-asset class investment vehicle as a designated investment alternative for an ERISA plan, including any fees or expenses associated with the vehicle or any of its investments, is not by itself a breach of fiduciary duties under ERISA</p>	<p><b>UNDER REVIEW.</b> This legislation strives to remove barriers to private equity and other alternative investments, such as digital assets, in defined contribution plans. This would appear to expose retirement saving to a much higher level of risk for a questionable reward. Congress should rely on the Department of Labor to make these sorts of judgments after study regarding the potential impacts.</p>
Section 401: Small Entity SEC Update Act		
<p>118<sup>th</sup> Congress                      + <a href="#">H.R. _____</a> (Wagner)</p> <p>117<sup>th</sup> Congress                      + JOBS Act 4.0, <a href="#">Sec. 401</a></p>	<p>+ Directs the SEC, in consultation with the Small Business Capital Formation Advisory Committee, the Office of the Advocate for Small Business Capital Formation, and the Office of Advocacy of the Small Business Administration, to conduct a study of the definition of the term “small entity” and publish a report to Congress with its findings and recommendations</p> <p>+ Directs the SEC to engage in rulemaking to implement its recommendations</p> <p>+ Directs the SEC to repeat the study every five years</p>	<p><b>QUALIFIED SUPPORT.</b> Congress should amend this legislation to require the SEC to consult with NASAA as well. For state securities regulators, small typically means America’s smallest businesses such as an ice cream store on Main Street. It does not mean an emerging growth company.</p>

Section 402: Increasing Opportunities for Retail Investors Act		
<p><b>117<sup>th</sup> Congress</b> + <a href="#">S. 3916</a> (Rounds)</p> <p><b>116<sup>th</sup> Congress</b> + <a href="#">H.R. 7834</a> (Hollingsworth)</p> <p><b>115<sup>th</sup> Congress</b> + <a href="#">H.R. 10</a> (Hensarling) + <a href="#">H.R. 4263</a> (MacArthur)</p>	<p>+ Authorizes the SEC to increase any statutory exemption ceiling, such as those governing offering sizes, if the SEC determines it appropriate</p>	<p><b>OPPOSE.</b> Congress already gave the SEC the authority to raise offering limits, and the Commission should be authorized to restrict, not just expand, existing exemptions. Instead of passing this legislation, Congress should direct the SEC to conduct, in consultation with NASAA, a holistic study on the U.S. capital markets. A holistic study would help the policymaking community make data-driven decisions on how best to restore the primacy of public markets in the United States and protect and empower investors.</p>
Section 403: Tracking Bad Actors Act of 2022		
<p><b>117<sup>th</sup> Congress</b> + <a href="#">S. 3716</a> (Kennedy)</p>	<p>+ Requires the SEC, CFTC, OCC, FDIC, FINRA, and PCAOB to jointly establish a database of persons convicted or held liable in criminal, civil, and administrative actions relating to financial services brought by the named regulators, the DOJ, any SRO overseen by the named regulators, or any state or local criminal or regulatory agency that voluntarily submits information to the database</p> <p>+ The database will be available to the public, free of charge</p> <p>+ Expungement from the database is required if the action is overturned upon judicial review or withdrawn by the agency</p>	<p><b>SUPPORT.</b> The proposed database would provide additional transparency to investors and likely would facilitate greater coordination among state and federal agencies. Before passing this legislation, Congress should revise the legislation to permit any state or federal government agency, such as a state securities regulator, or self-regulatory organization to make submissions to this database. In addition, Congress should revise the legislation to make clear that the database would include enforcement actions for institutions as well. Striving toward the use of a single, master database of public enforcement actions against individuals and institutions would save the government, financial services employers, and investors time and other resources.</p>

**Section 404: Protecting Investors' Personally Identifiable Information Act**

<p><b>117<sup>th</sup> Congress</b>                  + <a href="#">S. 1209</a> (Kennedy)                  + <a href="#">H.R. 2039</a> (Loudermilk)</p>	<p>+ Prohibits the SEC from requiring the use of personally identifiable information ("PII") to satisfy the reporting requirements of the Consolidated Audit Trail                  + As an "exception" to the above, permits the SEC to require a national securities exchange, association, or a member of either to provide PII with respect to a market participant if the SEC makes a request for such information</p>	<p><b>QUALIFIED SUPPORT.</b> We urge Congress to confine this bill to its primary objective: keeping PII out of the CAT database. Also, we urge Congress to make it clear that the legislation in no way limits or affects state investigative authority. Last, we urge Congress to explore opportunities to resolve related issues through oversight rather than legislation.</p>
--	---	--

**Section 405: Administrative Enforcement Fairness Act of 2022**

<p><b>117<sup>th</sup> Congress</b>                  + <a href="#">S. 3930</a> (Lummis)</p>	<p>+ Permits defendants in SEC administrative proceedings (except for registered entities like broker-dealers, investment advisers, and transfer agents) to transfer their case from the SEC to a federal district court</p>	<p><b>OPPOSE.</b> Giving respondents a right of removal would invariably slow the SEC enforcement process, add to the caseload of an already overburdened federal judiciary, and drive up taxpayer costs. It also may preclude the SEC from obtaining certain kinds of necessary relief authorized in the SEC's administrative enforcement forum, such as bars from association with registered broker-dealers and investment advisers.</p>
---	--	---

NASAA REPORT AND RECOMMENDATIONS FOR REINVIGORATING OUR CAPITAL MARKETS

Section 406: Registration for Index Linked Annuities Act		
<p><b>117<sup>th</sup> Congress</b> + <a href="#">S. 3198</a> (Smith) + <a href="#">H.R. 4865</a> (Adams)</p> <p><b>116<sup>th</sup> Congress</b> + <a href="#">S. 3795</a> (Smith) + <a href="#">H.R. 6994</a> (Phillips)</p>	<p>+ Requires the SEC to create a new form for the registration of index linked annuities and incorporate the results of investor testing when designing the form</p> <p>+ Defines a registered index linked annuity as an annuity that is deemed a security, which must be registered with the SEC, and that is issued by an insurance company subject to state supervision</p> <p>+ Includes a rule of construction to clarify that nothing in the bill can be construed to preempt state law</p>	<p>This legislation became federal law during the 117th Congress. NASAA agreed with the spirit and much of the substance of this legislation. We applaud lawmakers for their use of an express preservation of state authority clause in this legislation.</p>
Section 407: Alleviating Stress Test Burdens to Help Investors Act		
<p><b>117<sup>th</sup> Congress</b> + <a href="#">S. 5004</a> (Rounds) + <a href="#">H.R. 3412</a> (Loudermilk)</p> <p><b>116<sup>th</sup> Congress</b> + <a href="#">H.R. 3987</a> (Loudermilk)</p> <p><b>115<sup>th</sup> Congress</b> + <a href="#">S. 488</a> (Toomey) + <a href="#">S. 3574</a> (Rounds) + <a href="#">H.R. 4566</a> (Poliquin)</p>	<p>+ Exempts mutual funds and other types of non-bank financial companies from existing requirements <a href="#">under the Financial Stability Act of 2010</a> to conduct annual stress tests, which evaluate the ability of those companies to absorb losses as a result of adverse economic conditions</p> <p>+ Permits the SEC and the CFTC to require financial companies to conduct periodic stress tests</p>	<p><b>UNDER REVIEW.</b> The failure of nonbank financial institutions like Bear Sterns, Lehman Brothers, and AIG Insurance was among the events that precipitated the 2008-2009 Financial Crisis. Had such institutions periodically evaluated their capacity to absorb and manage losses in an adverse economic environment, we might have avoided considerable investor harm and grave danger to our economy. Congress should ensure that the SEC maintains a body of regulations that ensures the failure of a large asset manager cannot cause the next financial crisis.</p>



February 8, 2023

Chair Patrick McHenry  
Ranking Member Maxine Waters  
Members,  
House Committee on Financial Services  
2129 Rayburn House Office Building Washington, DC 20515

Dear Chair, Ranking Member and Members,

On behalf of more than 500,000 members and supporters of Public Citizen, we offer the following comment on three hearings and associated bills slated for consideration on February 8, 2023.

These three hearings are entitled "Revamping and Revitalizing Banking in the 21<sup>st</sup> Century;" "Sophistication or Discrimination? How the Accredited Investor Definition Unfairly Limits Investment Access for the Non-wealthy and the Need for Reform;" and "Empowering Entrepreneurs: Removing Barriers to Capital Access for Small Businesses." Each of these hearings bear on important subjects; that they should stumble over one another on the same day speaks to lack of sincere care accorded by the new majority leadership.

The premise by the majority in today's hearings is that entrepreneurs who want to start a bank and receive federal deposit insurance, (which insulates them from meaningful oversight by depositors who lend them money), should put less of their own capital in the bank. They also believe that investors in small start-ups should receive less information before they hand over money. These and other policies imbedded in these hearings are ill-advised.

Packed into these hearings are some 23 deregulatory bills, none of which will truly serve consumers or investors.

We address the bills as they are listed in the respective committee notices.

**At the hearing entitled "Sophistication or Discrimination? How the Accredited Investor Definition Unfairly Limits Investment Access for the Non-wealthy and the Need for Reform:"**

A suite of bills addresses the issue of accredited investors, which is a class of individuals who have considerable funds and therefore are permitted to hear solicitations for complicated and high-risk opportunities given that they can better shoulder a loss than can a low-income individual.

The “Fair Investment Opportunities for Professional Experts Act” would expand the definition of “accredited investor” to include individuals with certain licenses and qualifying education or job experience; The “Equal Opportunity for All Investors Act of 2023” expands the definition of “accredited investor” to include individuals that are certified through an examination established by the Securities and Exchange Commission (SEC); The “Accredited Investor Definition Review Act” requires the SEC to review the list of certifications, designations, and credentials for individuals to qualify as an accredited investor and add additional certifications, designations, and credentials to such list which the SEC determines are substantially similar to the existing ones within 18 months and every five years thereafter; The “Accredited Investor Self-Certification Act” requires the SEC to create a form that would allow individuals to qualify as an “accredited investor” by self-certifying that they understand the risks of investment in private issuers; The “Investment Opportunity Expansion Act” expands the definition of “accredited investor” to include individuals who invest 10% or less of the greater of their net assets or annual income in a private offering; An untitled bill would expand the definition of “accredited investor” to include individuals receiving individualized investment advice or individualized investment recommendations with respect to a private offering from a professional who qualifies as an accredited investor.

We generally oppose this suite of bills, as they would expose a greater number of vulnerable people to high-risk schemes. We do support greater study of how the SEC should protect vulnerable investors who sure not be lured into high stakes ventures while allowing others with market savvy to explore complicated offerings. We also believe the SEC should increase the minimum level of income and assets that qualify an individual as “accredited,” as inflation has debased the current figure.

The “Increasing Investor Opportunities Act” amends the Investment Act of 1940 to allow a closed-end fund to invest up to all its assets in private funds. Private funds have become a danger to a capital market that depends on disclosure, a conspicuously missing element in this sector. Private funds have no need for additional funds, and mutual funds, which attract small investors, should not be an additional funnel of financial resources. We oppose this bill.

The “Gig Worker Equity Compensation Act” expands Securities Act Rule 701 to include gig workers and preempt state laws that mischaracterize gig workers as employees. Gig workers already suffer from inferior worker standards and should not be excluded from what state laws that do apply in this misleadingly titled bill. We oppose this bill.

**At the hearing entitled “Revamping and Revitalizing Banking in the 21st Century:”**

The “Financial Data Privacy Act” amends the Gramm-Leach-Bliley Act to provide anemic additional protections at a high cost to consumers. The bill prevents states from tailoring protections to their residents or making stronger standards, and dangerously limits the rights of consumers to sue when they have been injured. While privacy protections are urgently needed in the financial space and across the board, this bill is not protective enough to justify the anti-consumer enforcement provisions. A truly protective bill would mandate data minimization, outline a permissible use framework, and provide robust private rights of action while allowing states to make stronger laws. Public Citizen opposes this bill.

The “Promoting Access to Capital in Underbanked Communities Act” would attempt to increase de novo bank formations by reducing initial capital requirements. This is misguided. Banking, unlike any other industry, depends on federal taxpayer backing of depositors. That means the depositor—who loans money to a bank—need not perform normal due diligence about management. Even if the management is incompetent, even if bad management drives the bank into insolvency, the depositor will be repaid. Because of this, banking must maintain high standards. This means that entrepreneurs who want to start a bank must put in substantial capital. To reduce these standards to spur greater bank creation simply invites the unscrupulous to infiltrate the industry. We oppose this bill.

The “Bank Service Company Examination Coordination Act” would require coordination of state banking agencies and federal banking agencies in regulating and examining the activities of bank service companies. This bill allows for information sharing on examinations and regulations between federal and state agencies and additionally requires that state and federal agencies coordinate and avoid duplicative examination activities, reporting requirements, and requests for information. We support coordination, but we believe that banks should face greater, not fewer examinations, and oppose this bill.

The “Promoting New and Diverse Depository Institutions Act” directs the federal banking agencies to conduct a study regarding the barriers to entry that de novo depository institutions face, and subsequently requires a strategic plan to be generated by the agencies, based on the findings of the study, which provides for the promotion of de novo applicants. Specifically, the strategic plan is intended to focus on the promotion of minority depository institutions, entities that could be certified as community development financial institutions, and depository institutions in underserved communities. We support this bill.

The “Financial Stability Oversight Council Improvement Act” prevents the Financial Stability Oversight Council (FSOC) from voting to determine that a nonbank financial company will be supervised by the Board of Governors of the Federal Reserve System without first considering alternatives. Specifically, the FSOC must determine, in consultation with the company in question and the company’s primary financial regulator, that heightened standards and safeguards, or a separate written plan submitted to the FSOC, is insufficient to mitigate the threat posed by the company to U.S. financial stability. This unwise bill would shackle federal regulators who should be looking carefully at the mammoth shadow banking sector. Firms such as AIG, a shadow bank, required the largest bailout during the 2008 financial crisis. Other behemoths may loom on the horizon as systemic threats. The FSOC statute provides for closer examination of any firm whose failure would pose a national danger. The statute does not call for supervision only after failure. We strongly oppose this bill.

**At the hearing entitled “Empowering Entrepreneurs: Removing Barriers to Capital Access for Small Businesses:”**

The “Improving Crowdfunding Opportunities Act” preempts state regulation of secondary transactions involving crowdfunding vehicles and clarifies legal liability for crowdfunding portals. It also increases the allowable aggregate amount companies can raise in any 12-month period from \$5 million to \$10 million and allows all non-accredited investors to invest up to 10% of the greater of their annual income or net worth. This bill also allows investment companies to participate in crowdfunding offerings and increases

the offering size threshold under which an issuer may meet its financial statement requirements. Preempting state oversight would shield fraudsters from a vital investor watchdog. We oppose this bill.

The “Small Entrepreneurs Empowerment and Development (SEED) Act” provides small issuers with a micro-offering exemption free of mandated disclosures or offering filings, but subject to the antifraud provisions of the Federal securities laws. Investors in smaller companies need more information, not less, given that these are largely untested enterprises without a larger shareholder base that serves as more effective overseers. We oppose this bill.

An untitled bill would preempt blue sky laws for off-exchange secondary trading in companies who make available current public information. State securities laws, or “blue sky laws” provide basic protections from fraud. We oppose this bill.

Another untitled bill directs the SEC to update its definitions of “small entities” under the Regulatory Flexibility Act to ensure that the SEC more carefully accounts for impacts on small businesses when pursuing rulemaking. We oppose this bill.

The “Developing and Empowering our Aspiring Leaders Act” requires the SEC to revise the definition of a qualifying investment, for purposes of the exemption from registration for venture capital fund advisers, to include equity securities issued by qualifying portfolio companies as well as investments in other venture capital funds. We believe that venture capital funds should provide additional disclosures and do not support such an exemption, and oppose this bill

The “Improving Capital Allocation for Newcomers Act” modifies the Qualifying Venture Capital Fund Exemption by increasing the cap on aggregate capital contributions and uncalled capital commitments from \$10 million to \$150 million and increasing the allowable number of beneficial owners from 250 to 600. We believe schemes that involve a greater number of investors in high risk, low disclosure ventures fail to honor basic protections. We oppose this bill.

The “Regulation A+ Improvement Act” increases the offering amount that companies can raise under Regulation A from \$50 million to \$150 million, adjusted for inflation by the SEC every two years to the nearest \$10,000. Low disclosure ventures must be discouraged, as is the case with Regulation A offerings. We oppose this bill.

The “Unlocking Capital for Small Businesses Act” directs the SEC to finalize its 2020 proposed exemption from broker registration requirements for “finders” who help issuers raise capital in private markets from accredited investors. We do not support exemptions for “finders” who may bring conflicts of interest to their recommendations and oppose this bill.

The “Helping Angels Lead Our Startup Act” defines an angel investor for purposes of the federal securities laws. It also clarifies the definition of general solicitation contained in the Securities Act to ensure that startups can discuss their products and business plans at certain events, known as “demo days,” without such discussions being considered an investment offering. We oppose sales events for small enterprises without appropriate disclosures and oppose this bill.

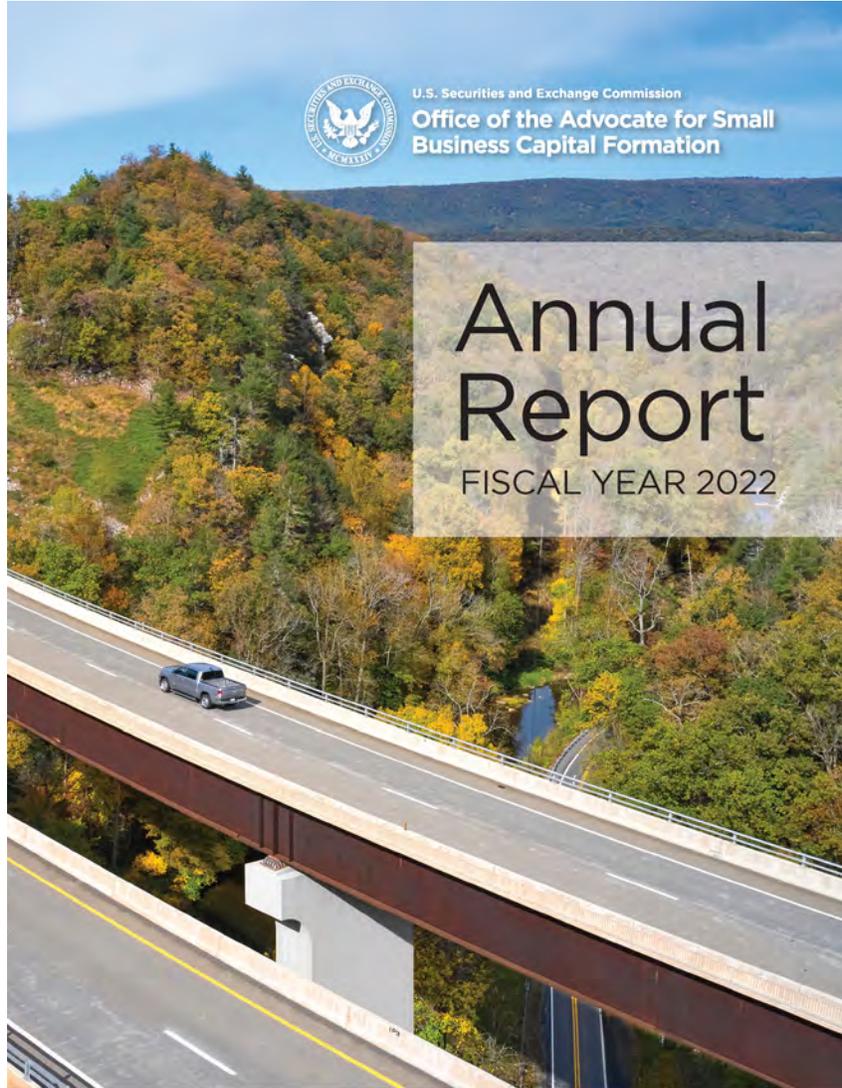
An untitled bill amends the Investment Advisers Act of 1940 to increase the exemption from registration threshold for certain investment advisers of private funds. Again, we supporter greater and not less information and oppose this bill.

Again, the many bills offered in this hearing make clear that the majority is focused on gutting investor and consumer protection in the service of Wall Street. Were the new leadership truly interested in serving America, they would hold urgent hearings on the scam that is cryptocurrency, the need to help the unbanked, runaway executive pay and any number of legitimate issues that concern average citizens.

For questions, please contact Bartlett Naylor at [bnaylor@citizen.org](mailto:bnaylor@citizen.org). For questions about the Financial Data Privacy Act, please contact Emily Peterson-Cassin at [epetersoncassin@citizen.org](mailto:epetersoncassin@citizen.org).

Sincerely,

Public Citizen



**ABOUT THIS REPORT + ACKNOWLEDGEMENTS**

This annual report of the Office of the Advocate for Small Business Capital Formation for Fiscal Year 2022 is being delivered to the Committee on Banking, Housing, and Urban Affairs of the U.S. Senate and the Committee on Financial Services of the U.S. House of Representatives in accordance with Section 4(j) of the Securities Exchange Act of 1934 (the Exchange Act), as amended by the SEC Small Business Advocate Act of 2016, 15 U.S.C. § 78d(j)(6).

Pursuant to Section 4(j)(6)(D) of the Exchange Act, this Report is provided directly to the committees of Congress without any prior review or comment from the Commission, any Commissioner, any other officer or employee of the Commission, or the Office of Management and Budget. It does not necessarily reflect the views of the Commission, the Commissioners, or staff of the Commission.

The work of the Office is possible only through the support of our talented and passionate colleagues across the agency. The Office owes special thanks to our colleagues who provided resources for this Report, including the Division of Economic and Risk Analysis for providing data to quantify the state of small business capital formation and contextualize issues, and the Office of Public Affairs for making our written product for this report visually engaging. We particularly thank the following individuals: Daniel Bresler, Mariesa Ho, Angela Huang, Olga Itenberg, Vladimir Ivanov, Andy Kim, Rey-Er Lee, Wei Liu, Richard Oliver, Chris Onrubia, Elizabeth Phillips, Lisa Pulaski, Zehra Sikandar, Erin Smith, Brian Ward, and Huaiqiang (John) Zheng.

## Message from the Small Business Advocacy Team

It has been another challenging year for small businesses. While the most significant hardships brought by COVID-19 appeared to lessen, many small businesses were simultaneously forced to confront a host of new issues. This year has brought an acute awareness of disruptions to supply chains, rising interest rates, inflationary pressures, a constrained labor market, and heightened geopolitical conflicts.

For small businesses looking to raise capital, the “banner year” we discussed in our 2021 annual report quickly faded away. Raising investment capital became harder at every stage of the capital raising cycle. The challenges for underrepresented founders were even further magnified.

Now, more than ever, it is important to focus on the need for strong connections between founders and the investors looking to support them, as reflected in the visual theme of this year’s annual report: building bridges. We call on Congress, the Commission, and our partners to support small businesses and their investors, with a particular focus on underrepresented founders and their investors.

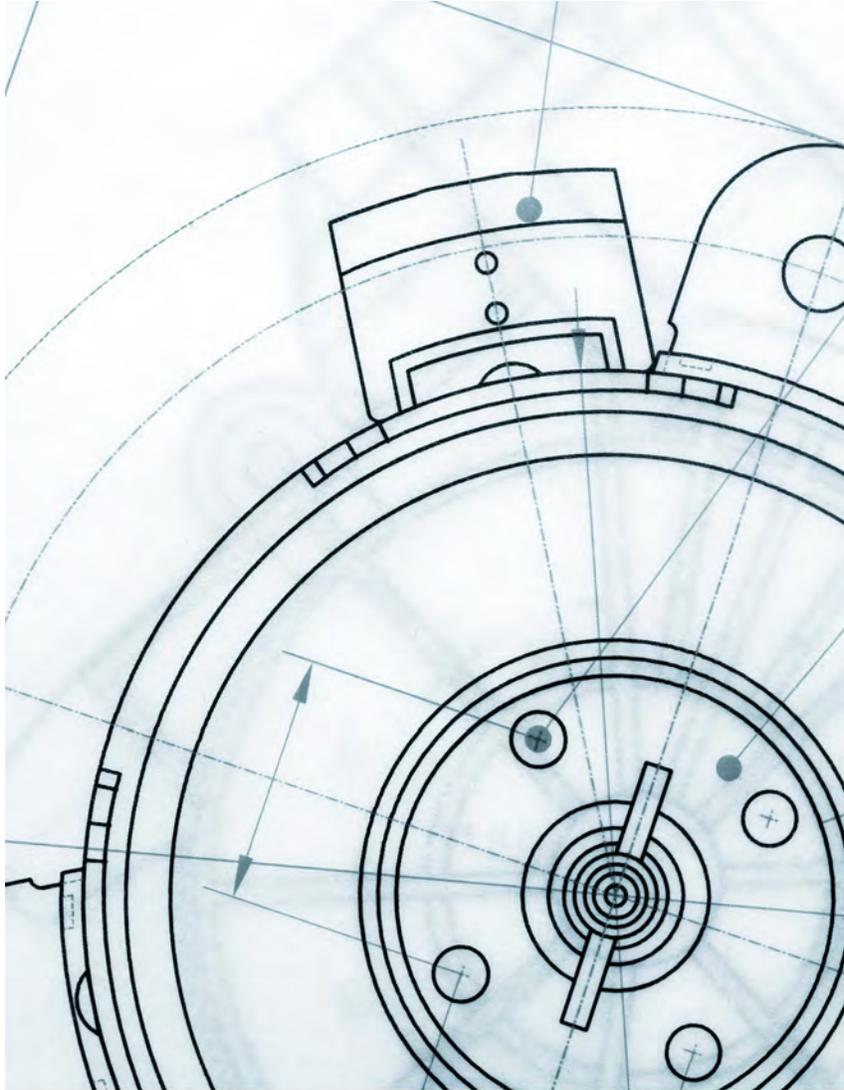
On a more personal note, this year brought the departure from the SEC of Martha Legg Miller, the inaugural Director of the Office. Martha brought wisdom, vision, and creativity, all of which have come to define the work of the Office. Each of our annual reports has endeavored to embody those qualities. Martha’s legacy is extensive and wide ranging—from our novel and interactive educational resources that break down the securities laws and empower entrepreneurs and their investors, to behind-the-scenes advocacy for policy changes that gave a voice within the Commission to entrepreneurs and investors alike. Thank you, Martha, for your public service. We hope this year’s report shows that we are proud to continue passionate advocacy for small businesses and their investors!





# Contents

ABOUT THE OFFICE . . . . .	1
HIGHLIGHTS FROM FISCAL YEAR 2022 . . . . .	4
STATE OF SMALL BUSINESS CAPITAL FORMATION . . . . .	13
Small and Emerging Businesses . . . . .	22
Mature and Later-Stage Businesses . . . . .	31
Small Public Companies . . . . .	39
Women Business Owners and Investors . . . . .	45
Minority Business Owners and Investors . . . . .	54
Natural Disaster Areas . . . . .	62
Rural Communities . . . . .	64
POLICY RECOMMENDATIONS . . . . .	69
Entrepreneurs and their investors need accessible tools and educational resources to navigate complex securities laws. . . . .	70
Targeted regulatory changes can improve access to capital . . . . .	72
Connecting founders with savvy investors is essential to capital raising. . . . .	76
Emerging fund managers play a key role in small business capital formation and need support. . . . .	78
Scaled disclosures for small public companies help them stay public. . . . .	81
SMALL BUSINESS CAPITAL FORMATION ADVISORY COMMITTEE FY2022 SUMMARY . . . . .	85
ENDNOTES . . . . .	93



## About the Office

The Office advocates for solutions to address challenges faced by small businesses and their investors raising and deploying capital. “Small business” for the Office spans from early-stage startups raising seed capital, to later-stage private companies whose founders and investors are seeking liquidity in the public markets, all the way to smaller public companies. Congress established the Office via the bipartisan [SEC Small Business Advocate Act of 2016](#) as an independent office within the U.S. Securities and Exchange Commission (SEC) that reports to the entire Commission as well as to multiple committees of Congress.

The Office approaches its advocacy mission by:

- Engaging with small businesses and their investors to understand their most pressing capital raising issues;
- Identifying unique capital raising challenges faced by minority-owned, women-owned, rural, and natural disaster-affected small businesses and their investors;
- Analyzing the potential impact of policy changes likely to significantly affect small businesses and their investors; and
- Advocating to Congress and the Commission for policy changes.

### Mission

We champion pragmatic solutions so that small businesses—from startups to smaller public companies—and their investors can build great companies together using our capital markets.

### Core Values

- **ACCESSIBILITY** — We engage with both small businesses and their investors, as well as with the SEC, SROs, Congress, and other agencies on a regular basis through a variety of channels.
- **INCLUSIVITY** — We encourage people to speak openly and contribute authentically to facilitate greater trust and collaboration.
- **PRAGMATISM** — We approach problems with a solution-oriented mindset to make practical recommendations.
- **EFFICIENCY** — We operate like a lean startup, maximizing resources and focusing activities where the Office can have a meaningful impact.

Our Advocacy Team



SEBASTIAN GOMEZ  
ABERO  
*Deputy Director*



JOHN CAVANAGH  
*Special Counsel*



JENNY J. CHOI  
*Special Counsel*



JULIE ZELMAN  
DAVIS  
*Senior Special Counsel*



KIM DINWOODIE  
*Engagement Specialist*



COURTNEY  
HASELEY  
*Special Counsel*



SARAH R. KENYON  
*Capital Formation Analyst*



JEPHTE LANTHIA  
*Special Counsel*



VIKKI PORTER  
*Visual Design Strategist*



AMY REISCHAUER  
*Strategic Engagement  
Advisor*



JENNY RIEGEL  
*Policy Manager*



MALIKA SULLIVAN  
*Executive Assistant*



TODD VANLAERE  
*Law Clerk*

### FY2022 at a Glance

We engage with small businesses and their investors from around the country to hear their perspectives on issues facing the small business ecosystem, from policy, to changing trends in capital raising, to the complexities of the capital raising regulatory framework, to unique challenges and opportunities of different demographic groups and geographic regions. The insight we gain from our events and conversations with small business ecosystem participants provides timely, practical feedback to inform the Commission's policymaking as well as the Office's further outreach and educational efforts.

Our reach extends coast to coast, across media platforms, and to a range of partners and organizations.



Our educational resources cover a range of topics, are easily accessible, and are expanding.



**1** CAPITAL RAISING HUB for all SEC small business resources

**24K+** VISITS to the CAPITAL RAISING HUB 

**119K+**  views of our EDUCATIONAL TOOLS and SMALL BUSINESS RESOURCES



**1** NAVIGATOR TOOL to explore many pathways to capital

**10** BUILDING BLOCKS



**68** TERMS in our expanded CUTTING THROUGH THE JARGON glossary

**3** YEARS OF DATA in our interactive CAPITAL TRENDS MAPS 

**8** new EDUCATIONAL VIDEOS 

## Outreach and Engagement

This year, we had opportunities to connect in person at outreach events and in small group gatherings. We also continued to leverage the benefits of remote engagement by reaching diverse audiences across the small business ecosystem and across the country through virtual events and speaking engagements. We found opportunities to share information about our Office's resources, programs, and services and to hear from small businesses, their investors, and other thought leaders in the market.

Entrepreneurs shared their challenges and successes building and funding their businesses.

[Starting a business] is very tough. You have to have a passion for it. You have to believe in yourself and never accept no for an answer.

— **DOKMAI WEBSTER**, *Founder and CEO*,  
Pivotal Point LLC



We heard from women and minority entrepreneurs about the unique challenges they face and how obstacles to capital raising are heightened for underrepresented groups.



One struggle for a lot of underrepresented founders is that many don't have mentors. If only two percent of venture dollars are going to Black and minority founders, then there aren't that many to get advice from. Without that network and the advice of people who have been there before, [new founders] can't get there.

— **DAVE LU**, *Founder and Managing Partner*,  
Hyphen Capital

Founders and investors across the country shared insights about the challenges and opportunities of raising capital outside of the traditional hubs.

As [local entrepreneurial ecosystems] develop and the number of firms increase over time in an area, you develop a critical mass that then makes it easier to attract subsequent investment.

— **MARYANN FELDMAN**, *Watts Endowed Professor*,  
Arizona State University



We engaged with fund managers, investors, and entrepreneurs on how to increase diversity among capital allocators and the impact it could have on underrepresented founders.

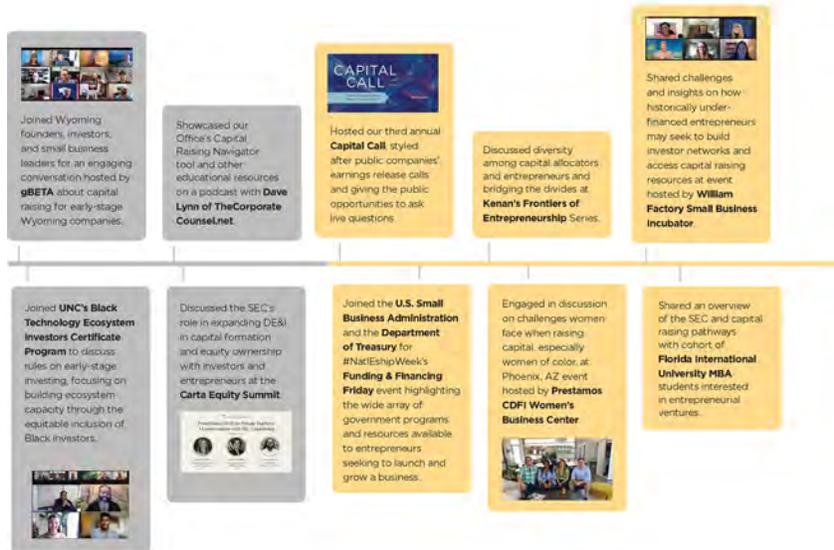


As a woman who has had success and came from very humble beginnings, it's my responsibility to recruit more women and people of color to invest. Because research shows that if you have more women and people of color investing, more women and people of color get funded.

— **CAROLINE CUMMINGS**, *CEO*,  
Regional Accelerator & Innovation Network (RAIN)

Highlights from FY2022

Some of the events in which we have engaged this year include:





### 41st Small Business Forum

The SEC's annual Small Business Forum is a unique event where members of the public and private sectors gather to provide feedback to improve capital raising policy.<sup>11</sup> The Forum covers a broad range of issues affecting small businesses and their investors, from early-stage entrepreneurial ventures to smaller public companies.

This year marked the 41st Forum, which the Office hosted virtually over four days from April 4-7, 2022. Each day featured speakers with in-depth knowledge of the issues facing small businesses across the country, spotlighting the following topics:



At the end of each day's session, participants prioritized policy recommendations on that topic to be submitted to the SEC and to Congress. Video archives of each day's events are available in the [Forum video gallery](#).

On July 28, 2022, the Commission delivered the 2022 [Forum Report](#) to Congress, which summarizes the Forum proceedings, including the recommendations developed by participants for changes to the capital raising framework and the Commission's responses to those recommendations.

## CAPITAL RAISING HUB

### Educational Tools and Resources

In the fall of 2021, in partnership with other SEC offices and divisions, we launched our Capital Raising Hub,<sup>2</sup> a centralized portal for educational tools and resources for entrepreneurs and their investors. We have continued to expand and update the Capital Raising Hub in response to feedback from small businesses and investors to make it easier to find all of our small business resources. In addition, the Capital Raising Hub is now directly accessible under the "Education" tab on the SEC's homepage. Visitors to the Hub will find resources to support each phase of the capital raising journey.



#### Getting Started: Understanding the Fundamentals



#### Navigate Your Options

We have continued to improve our interactive tool that explores regulatory pathways to raise capital, identifying the most relevant options based on the user's answers to a series of questions about their business.



#### Cutting Through the Jargon

We also have expanded our curated glossary of key terminology that makes the language of capital raising more accessible to small businesses and their investors.



#### Building Blocks

This year, we launched the first of several installments of our suite of educational materials that break down fundamental securities law concepts into plain language. We have continued to expand this collection of resources based on feedback received directly from prospective users through our outreach efforts.



#### Capital Raising Video Gallery

As part of the expansion of our Capital Raising Hub, we launched our new Capital Raising Video Gallery, where users can find a number of educational videos, including our Capital Raising 101 series and other videos highlighting pertinent capital raising topics and data.



 **The Landscape:**  
Data, Research, and Other Resources

 **Capital Trends Maps**  
We regularly update the data available through our interactive maps to allow users to stay informed about how and where capital is being raised across the country.

 **Research Reports**  
Reports and studies on capital raising issues and trends from around the country are also available.

 **Small Business Compliance Guides**  
Our comprehensive Capital Raising Hub affords easy access to the SEC's small business compliance guides, which provide valuable information on SEC rules on offering and selling securities and financial and other reporting by public companies and how they may affect smaller businesses.



## State of Small Business Capital Formation

The data provided in this Report is derived from public filings with the SEC, as analyzed by the SEC's Division of Economic and Risk Analysis (DERA), and is supplemented with figures and findings from third parties. We hope this approach provides a comprehensive snapshot of the state of U.S. small business capital formation, amalgamating many important pieces of the capital formation story into one resource to aid in evaluating the current flow of capital between investors and small businesses. The data supplements anecdotal evidence and helps quantify the successes and challenges in small business capital formation nationwide. Unless otherwise indicated, the data period for DERA data is July 1, 2021 to June 30, 2022. Using data, we can better identify what tools, strategies, and approaches would be most helpful in crafting policy solutions.

What regulatory pathways are companies using to raise capital?<sup>3</sup>



## What pathways are available to raise capital from investors?

### EXEMPT OFFERINGS

Offerings conducted pursuant to an exemption from registration are often referred to as exempt offerings. There are multiple exemptions available for small businesses looking to raise capital from investors.



**Rule 506(b) Private Placements** allow companies to raise unlimited capital from investors with whom the company has a relationship and who meet certain wealth thresholds or have certain professional credentials. A company cannot use general solicitation in a 506(b) private placement.<sup>5</sup>



**Rule 506(c) General Solicitation Offerings** allow companies to raise unlimited capital by broadly soliciting investors who meet certain wealth thresholds or have certain professional credentials.<sup>6</sup>



**Rule 504 Limited Offerings** allow companies to raise up to \$10 million in a 12-month period, in many cases from investors with whom the company has a relationship.<sup>7</sup>



**Regulation Crowdfunding Offerings** allow eligible companies to raise up to \$5 million in investment capital in a 12-month period from investors online via a registered funding portal.<sup>8</sup>



**Intrastate Offerings** allow companies to raise capital within a single state according to state law. Many states limit the offering to between \$1 million to \$5 million in a 12-month period.<sup>9</sup>



**Regulation A Offerings** (sometimes called a "mini-IPO") allow eligible companies to raise up to \$20 million in a 12-month period in a Tier 1 offering and up to \$75 million in a 12-month period in a Tier 2 offering through a process similar to, but less extensive than, a registered offering.<sup>10</sup>

### REGISTERED PUBLIC OFFERINGS

A registered public offering is commonly used to describe an offer and sale of securities that has been registered under the Securities Act. Companies must file a registration statement with the SEC and may not sell the securities until the SEC declares the registration statement effective.



**Initial Public Offerings (IPOs)** provide an initial pathway for companies to raise unlimited capital from the general public through a registered offering. After its IPO, the company will be a public company with ongoing public reporting requirements.<sup>11</sup>

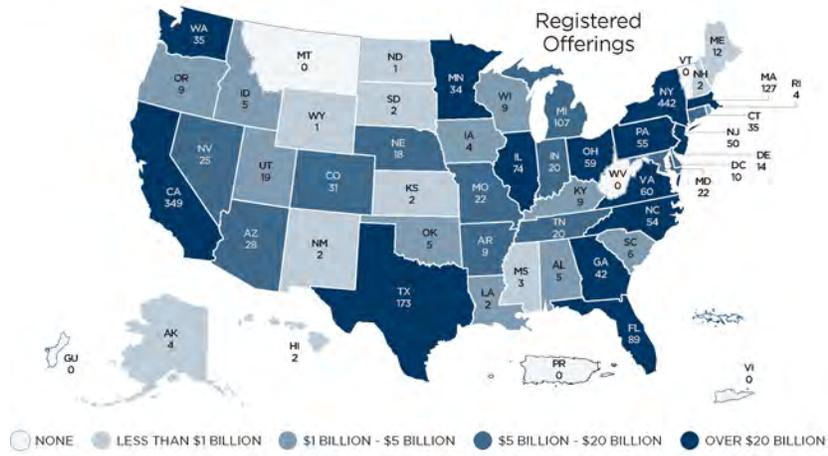
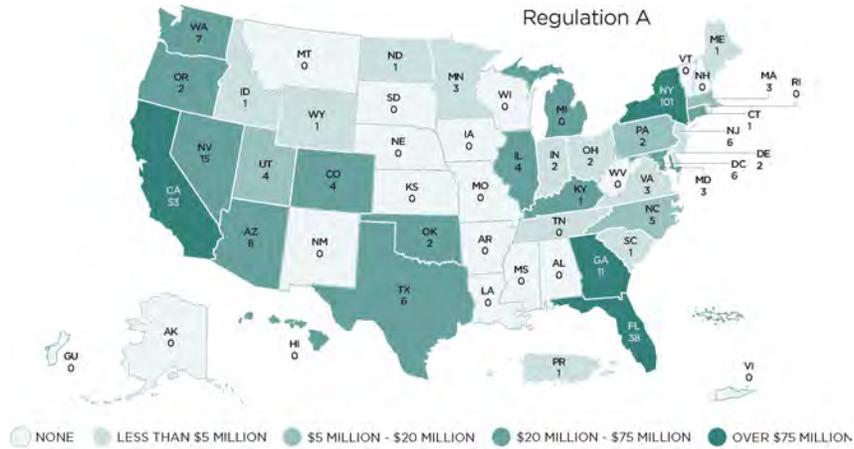


**Secondary Registered Offerings** allow companies to raise unlimited capital through secondary offerings using a registration statement filed with the SEC.<sup>12</sup>

How are different industries using the top 3 offering pathways to raise capital (excluding pooled funds)?<sup>13</sup>







### What is happening with Regulation Crowdfunding offerings?

The number and amount of crowdfunding offerings continue to increase, supporting more women-founded, minority-founded, and geographically diverse companies across the U.S.<sup>15</sup>



U.S. Counties with Crowdfunded Companies<sup>16</sup>



Quarterly New Crowdfunding Offerings<sup>17</sup>

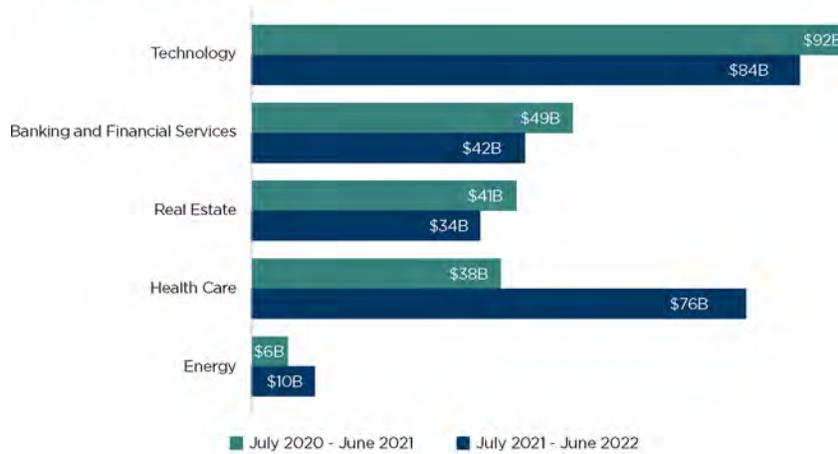


### What is happening with Regulation D offerings?

Pooled funds continue to account for over 85 percent of the funds raised under Regulation D.<sup>18</sup>



### What are the top industries raising capital through Regulation D (excluding pooled funds)?<sup>19</sup>

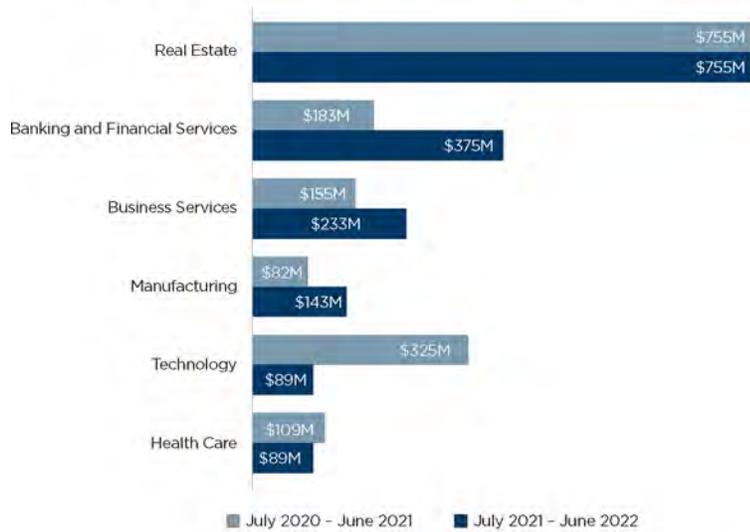


### What is happening with Regulation A offerings?

The amounts sought have declined following the peak in the third quarter of 2021.<sup>20</sup>



### What are the top industries seeking capital through Regulation A?<sup>21</sup>

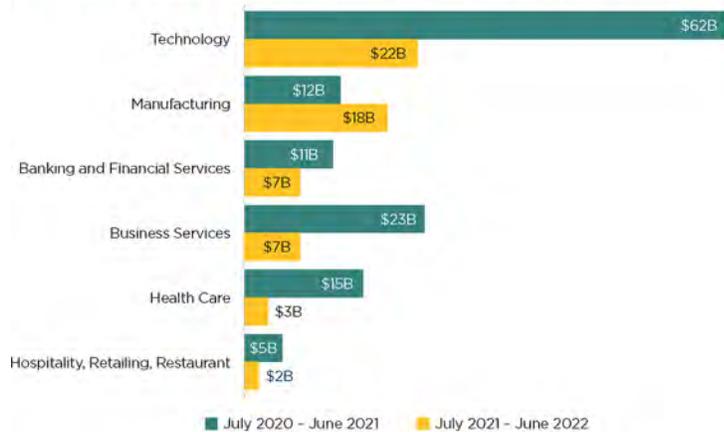


What is happening with IPO activity?

While 2020 and 2021 were busy years for the IPO market, there has been a downward trend in the first half of 2022 in terms of both volume and amount of initial public offerings and other public offerings.<sup>22</sup>



What are the top industries raising capital in IPOs (excluding pooled funds)?<sup>23</sup>



## Small and Emerging Businesses

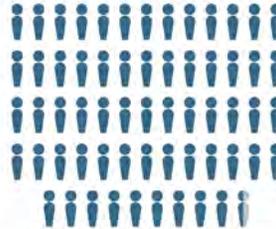
This segment of companies includes both high-growth startups that raise capital to get off the ground and launch early prototypes, as well as small businesses that create local jobs but may not fit the high-growth model that is the typical target of venture capital (VC) investments.<sup>24</sup>

Why is access to capital for small and emerging businesses so important?

Small businesses have an outsized impact on job creation.



**Small businesses** have accounted for 66% of employment growth over the past 25 years.<sup>25</sup>



**61.7 million Americans** are employed by a small business (46.4% of U.S. employees).<sup>26</sup>



Small businesses remain central to our society and the American dream. For the third year in a row, **the public has the most confidence in small businesses** out of 16 categories of major institutions in American society.<sup>27</sup>

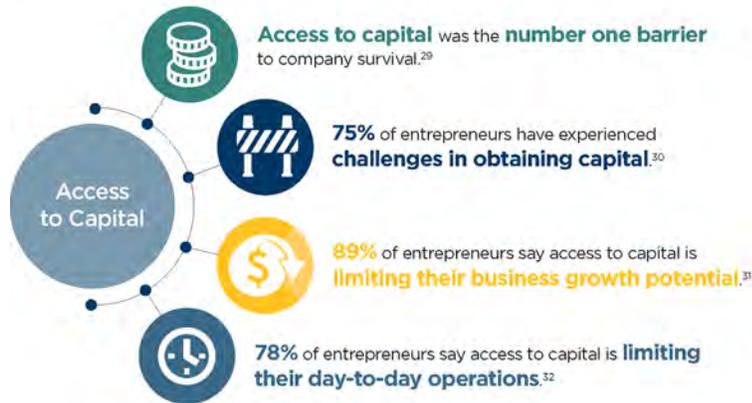
“

Capital remains among the most impactful ways to strengthen access to entrepreneurship ... When business owners do not have access to personal funds or quality capital, they are less able to take the risks necessary to grow their businesses, artificially stifling the marketplace.

EWING MARION KAUFFMAN FOUNDATION<sup>28</sup>

Early-stage entrepreneurs report struggles and need support as they build new companies

Access to capital remains a persistent barrier to growth for all entrepreneurs.



Entrepreneurs need support in accessing capital.



Bridging gaps between entrepreneurs and investors remains the biggest challenge for early-stage startups when raising capital.<sup>34</sup>



Robust ecosystems add to the success of early-stage startups.



Individuals with a mentor are **5X** more likely to plan to start a business than those who do not have a mentor.<sup>35</sup>



The introduction of **accelerators** to a region has a significant impact on the **number of early-stage deals** for new businesses.<sup>36</sup>

Several metrics of entrepreneurship have improved, but many small businesses have not recovered to prepandemic levels



In 2021, **5.4 million new business applications** were filed—more than 20% higher than any previous year on record.<sup>37</sup>

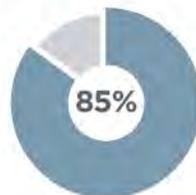


**74% of all counties** had more business establishments in Q3 2021 than they did prior to the pandemic.<sup>38</sup>



**82% of new startups** survived one year after founding (up from 78% in 2020 and 79% in 2019).<sup>39</sup>

An increasing percentage of small businesses are experiencing financial challenges.<sup>40</sup>



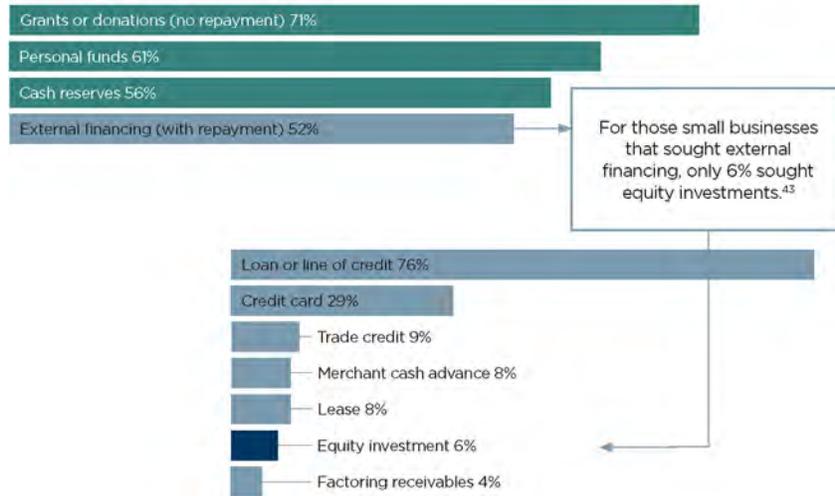
of small businesses **experienced financial challenges** in 2021 (up from 81% in 2020 and 66% in 2019).



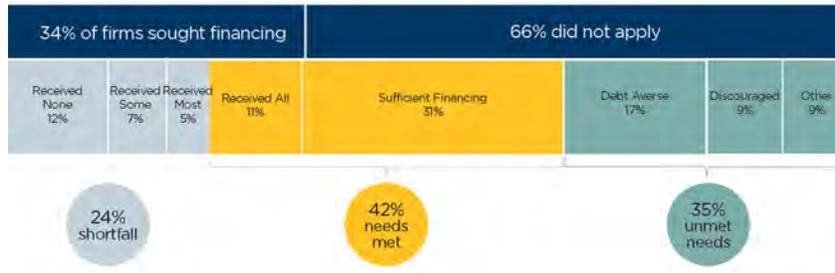
Many small businesses have not recovered to prepandemic levels, in terms of both revenue and employment, with the effects of the pandemic hitting disproportionately hard among firms in the leisure and hospitality sector, smaller firms, and firms owned by people of color.

FEDERAL RESERVE BANKS<sup>41</sup>

What are common sources of capital for small and emerging businesses when facing financial challenges?<sup>42</sup>



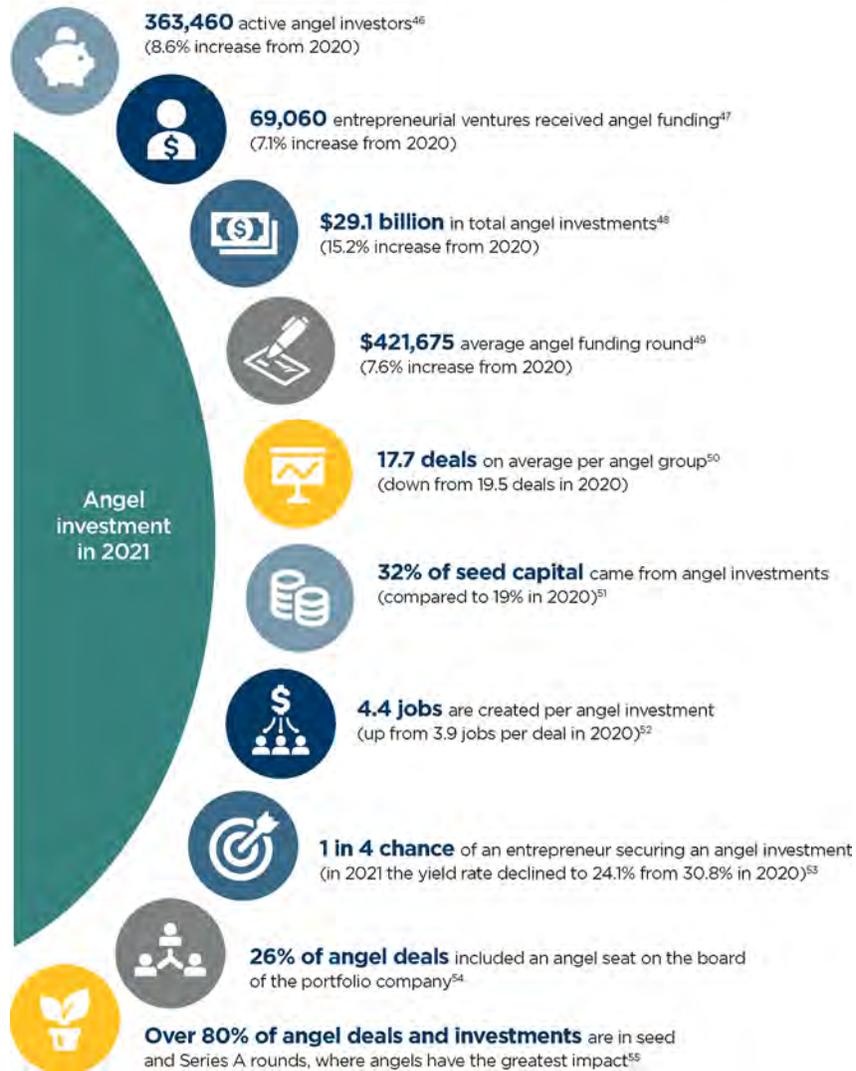
In 2021, fewer small businesses than in prior years received all of their requested funding or met their financing needs.<sup>44</sup>



Zooming in on the 34% of businesses that sought financing, **only 31% of these applicants received all of the funding they sought** (down from 36% in 2020 and 51% in 2019).<sup>45</sup>

## Angel investors continue to be a significant source of early-stage capital

Angel investors are generally high-net-worth individuals who invest their own money directly in emerging businesses, typically in early funding rounds. Most angel investors are accredited investors, and many are current or former entrepreneurs themselves.



### What is happening with seed fundraising?

A pre-seed or seed round is typically a company's first funding round. This round may include funding from friends and family, angel investors, or early-stage funds. Capital at this stage is often used for product development and market research.<sup>56</sup> Given the early stage, businesses in an angel or seed round are the furthest from the public market, insulating those companies from challenges arising in later stages of financing.<sup>57</sup>

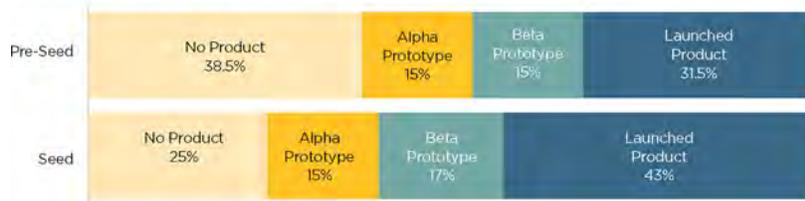
In recent years, the number of seed rounds and seed firms have increased.



Seed activity remained strong, despite a slight drop in deal counts.<sup>60</sup>



Early-stage businesses seeking pre-seed and seed funding are at different stages of product readiness.<sup>61</sup>



of pre-seed companies raised funding in 2021 and 2022 before launching a product (up from 8% in 2020).<sup>62</sup>

In 2021, how long did it take to fund pre-seed and seed rounds?<sup>63</sup>



The average pre-seed fundraising time **increased to 15 weeks** in the first half of 2022 (compared to 13.5 weeks in 2021).<sup>64</sup>

Since early 2022, pre-seed fundraising is becoming more competitive for founders in an investor-friendly market.<sup>65</sup>

**Investors**  
 ↓ **23%**  
 Less time engaging with pitch decks

**Founders**  
 ↑ **30%**  
 More pitch decks sent per week

What are the average costs of seed fundraising?<sup>66</sup>



**19.7%**  
 Average percent of equity sold to investors

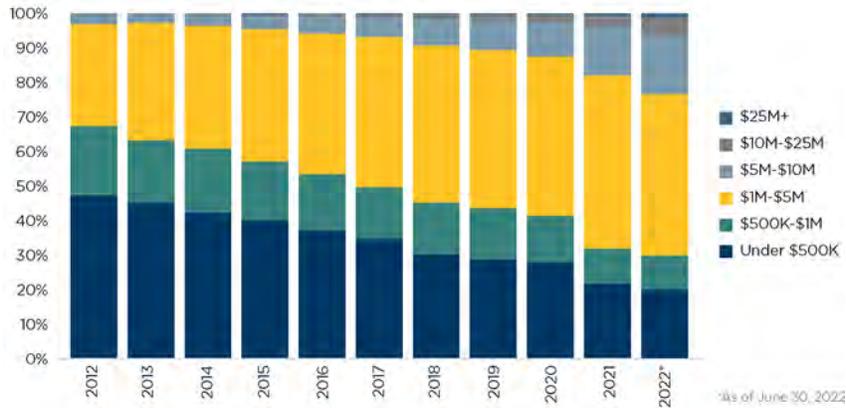


**10.1%**  
 Average amount of the equity allocated to the employee options pool



**\$28,800**  
 Average closing costs

While the average angel deal size in 2021 was \$421,675,<sup>67</sup> the vast majority of seed deals exceeded \$1 million.<sup>68</sup>

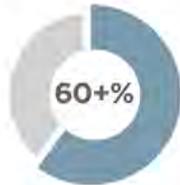


Micro funds – funds raising \$50 million or less – continue to strengthen seed activity.<sup>69</sup>



Over 1,600 micro funds have closed since the beginning of 2018, including nearly 200 in the first half of 2022.<sup>70</sup>

From 2018 to 2021, micro funds raised between \$4 and \$5 billion annually (representing 4% of the deal value but 40% of the deal count).<sup>71</sup>



60+% of micro funds are raised by emerging managers.<sup>72</sup>

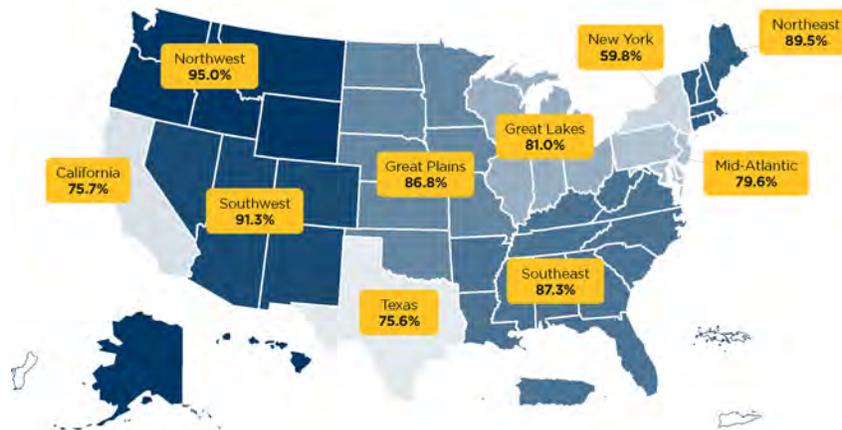


[T]he investment power of these small funds is multiplied by the networks they bring into new ecosystems. As more companies receive local investment, the growing cohort of companies will be able to draw capital from larger funds located in other areas. This itself is a major reason for needing local capital, as those firms will have a larger network and reach than many of the founders needing to raise capital.

KYLE STANFORD, PITCHBOOK<sup>73</sup>

Many early-stage investors continue to fund companies within their region<sup>74</sup>

The percentage of angel investments remaining within their region continues to increase.<sup>75</sup>



Seed funding has expanded into smaller ecosystems, but remains localized.<sup>76</sup>



The median distance between a company and a seed lead investor is **94 miles**.<sup>77</sup>

“

Access to capital is still fairly localized . . . Entrepreneurs and fundraisers outside of top-tier funding hubs often still face high capital-raising hurdles, and it becomes increasingly difficult to raise capital the farther you are from a city hub. Despite their smaller share of total investment dollars, however, regions outside these top 10 funding hubs accounted for more than a third of the number of angel and seed deals, representing a broad base of startup environments and untapped potential.

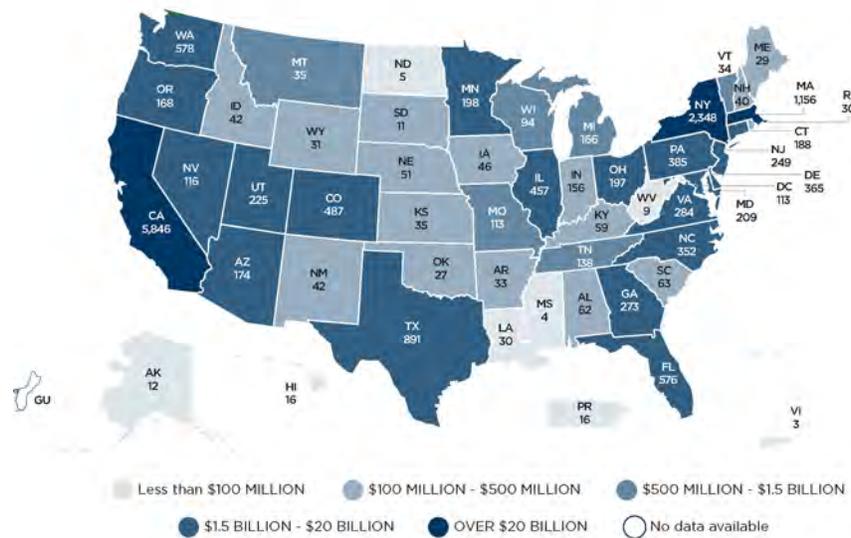
KENAN INSTITUTE OF PRIVATE ENTERPRISE<sup>78</sup>

## Mature and Later-Stage Businesses

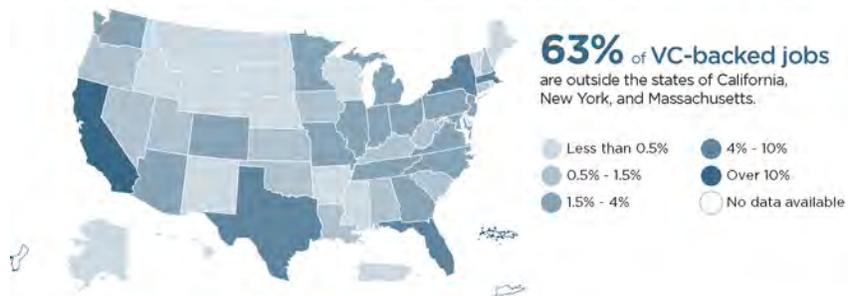
Companies within this segment of the market are generally growing and looking for larger amounts of capital that can fund operations of scale, ventures into new product lines, and preparation for public markets. Most often, their investors are institutional in nature, whether VC funds, private equity funds, or crossover investors from the public market.

### VCs fund growth startups across the country but untapped markets remain

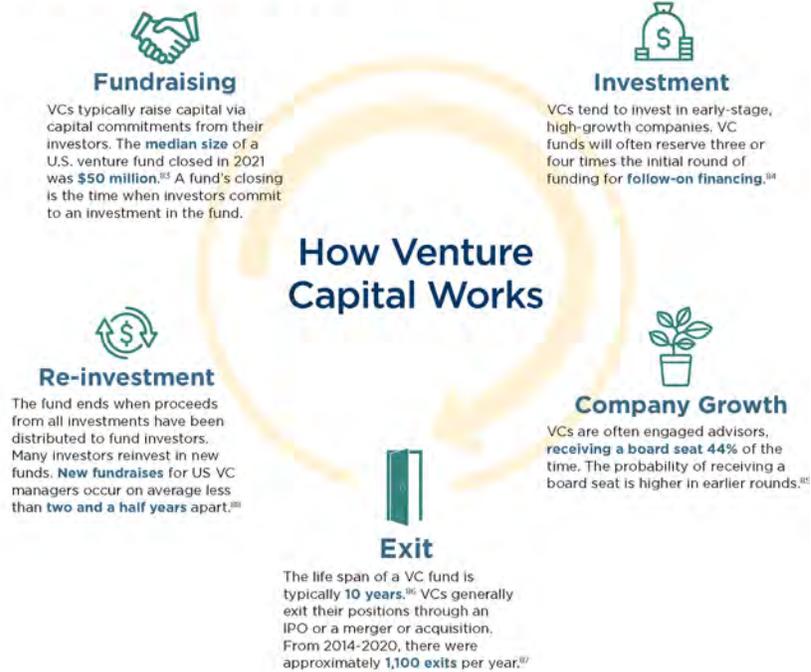
The below map illustrates the concentration of estimated VC deal value in 2021, with the number of VC deals indicated on each state.<sup>79</sup>



While 73% of VC funding remains concentrated in the top three states,<sup>80</sup> VC-backed jobs are more broadly distributed across the US<sup>81</sup>



What is the typical VC cycle?<sup>82</sup>



### How do VCs fund businesses across their lifecycle?



For any business that receives VC funding, the business's development will generally progress with its funding rounds.<sup>90</sup>



### How is VC investment activity changing?

VC funding reached record highs in 2021. 2022 has brought a variety of changes and challenges affecting companies and investors in the U.S. VC ecosystem, including concerns about inflation, rising interest rates, and a slowdown in the U.S. public markets.<sup>91</sup>

2022 VC deal value and deal count are historically high, even as they may fall short of record-breaking highs reached in 2021.<sup>92</sup>

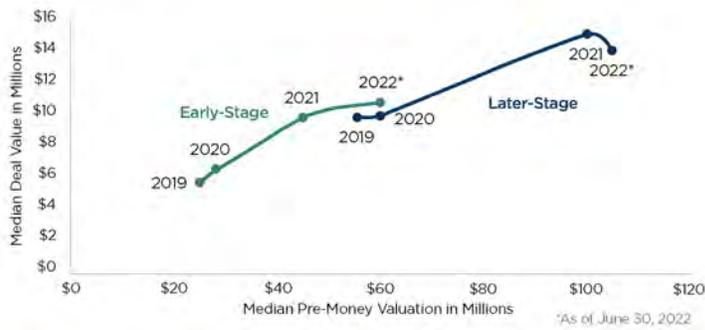


Later-stage investment volume peaked in 2021 but remains at heightened levels through the first half of 2022.<sup>93</sup>

VC investments in later-stage businesses over the first half of 2022 are approximately equal to investments made over the course of the full year in each of 2018 and 2019.



Later-stage pre-money valuations may have plateaued after a rapid rise in 2021.<sup>94</sup>



[M]any companies are buying time with bridge rounds, allowing them to extend their runways without a down round (a primary round at a lower valuation). These companies are waiting until their fundamentals or wider market conditions improve enough to have their valuation expectations met in an IPO or primary financing round.

LIAN CHANG, CARTA<sup>SM</sup>

### How is VC fundraising activity changing?

Billion dollar funds account for almost two-thirds of capital raised so far in 2022—already the second highest year on record for VC fundraising.<sup>96</sup>

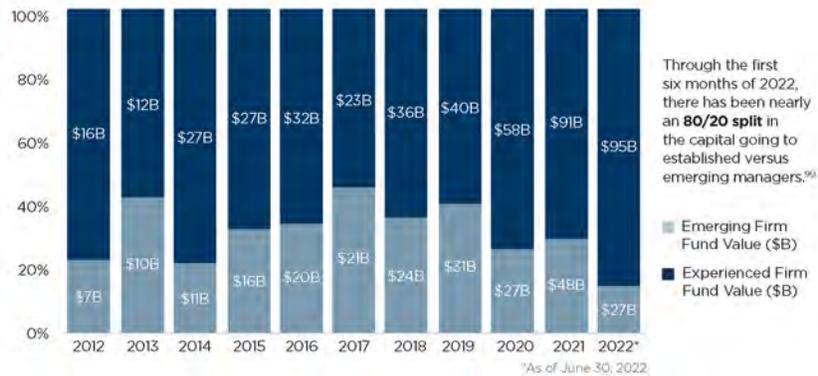
The below graph illustrates the amounts raised by VC funds of various sizes.



We expect emerging managers to have a more difficult time raising new funds over the near term as LPs rebalance their portfolio and allocate to known, or more established, investors and managers.

PITCHBOOK<sup>97</sup>

The percentage of capital going to emerging managers has declined to a new decade low.<sup>98</sup>



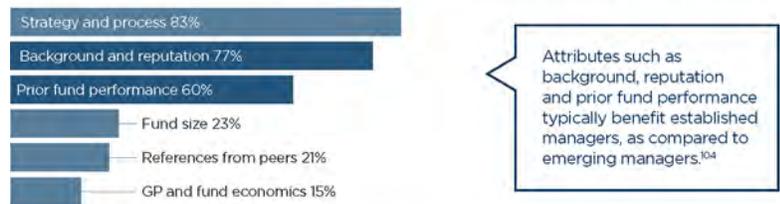
How are LPs considering, meeting, and evaluating new fund managers?



While many LPs are seeking new manager relationships, network connections remain the dominant pathway LPs use to meet new fund managers.<sup>101</sup>



What are the top factors LPs consider in evaluating new fund managers?<sup>103</sup>

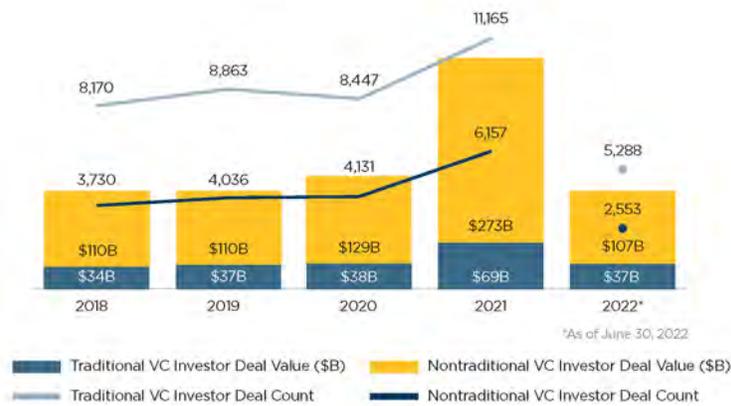


Emerging managers often differentiate themselves through in-demand strategies or a particular focus on a region or demographic. As more managers enter the ecosystem, finding out-of-network connections may become increasingly challenging.<sup>105</sup>

### What is the impact of nontraditional investors on mature and later-stage fundraising?

Over the last few years, nontraditional investors—generally firms and institutions not labeled as VCs—have increasingly crossed over from the public markets to invest in VC-backed companies.<sup>106</sup>

In recent years, the VC landscape has seen growth in deal sizes, valuations, and the number of mega-deals in which nontraditional investors participated.<sup>107</sup>



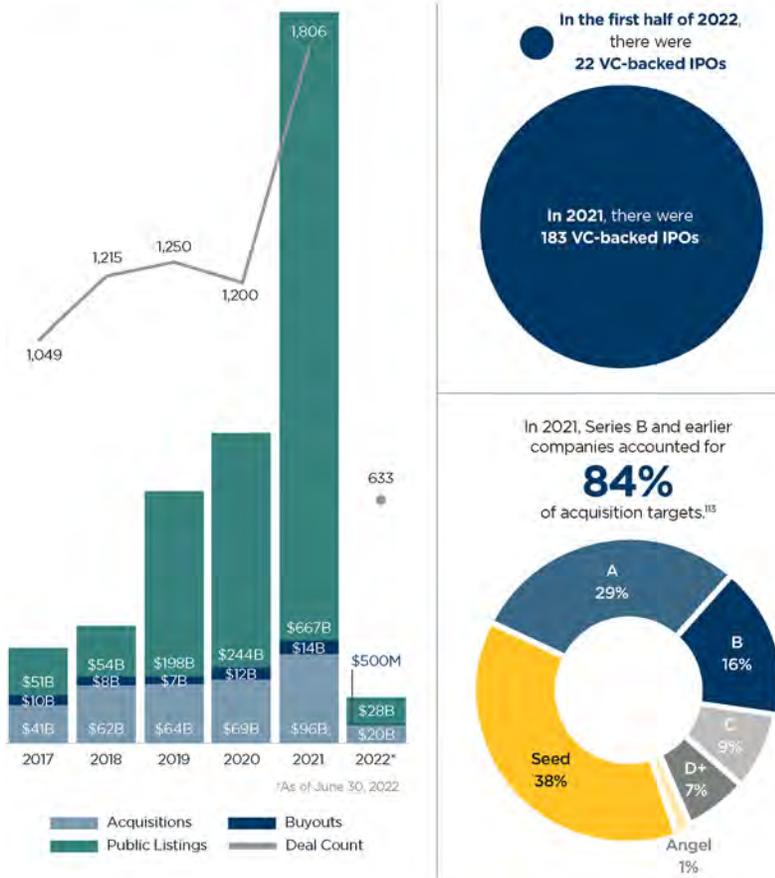
### Nontraditional investor participation in later-stage VC deals remains high.<sup>108</sup>



### Portfolio company exits fuel reinvestments by LPs into new VC funds

Reduced distributions to LPs as a result of the slowdown in the IPO market may disproportionately affect emerging fund managers, as LPs may be more inclined to allocate a now smaller pool of available capital to established managers.<sup>110</sup> Likewise, lower public market valuations could lead to an overweighting in the portfolios of LPs to private market investments.<sup>111</sup>

Venture-backed exit activity in the first half of 2022 has seen a significant decline in valuations as well as deal counts from 2021—reverting to 2017 and 2018 levels—with public listings leading the downturn.<sup>112</sup>



## Small Public Companies

Companies can access broad pools of investors when they conduct public offerings. This allows them to raise large amounts of capital to fund activities, such as research and development, capital expenditures, or debt service. Public offerings also provide liquidity to early-stage investors and employees.

How have U.S. exchange-listed companies changed over time?

The number of **small exchange-listed companies**<sup>114</sup> has **drastically declined** over the last several decades, while the number of large exchange-listed companies continues to increase.<sup>115</sup>



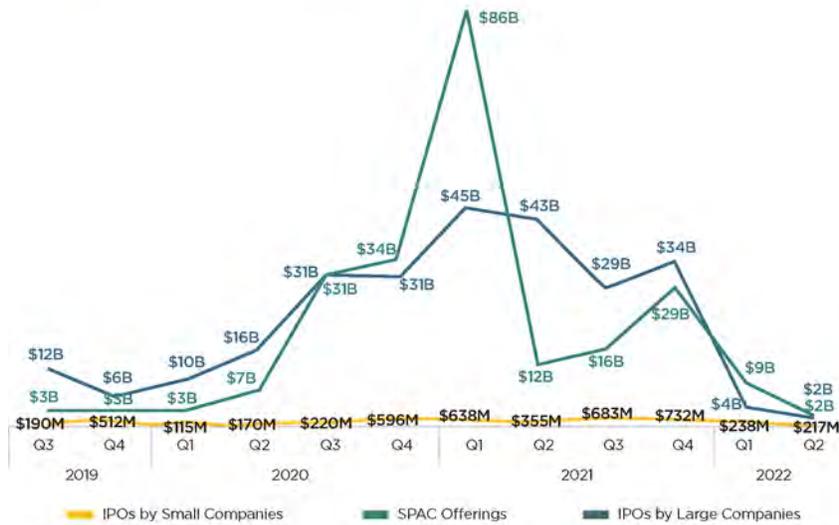
\*As of June 30, 2022

The aggregate market capitalization of small exchange-listed companies has faced an even steeper decline as a proportion of the overall market—with the percentage falling by half or more each decade.<sup>16</sup>

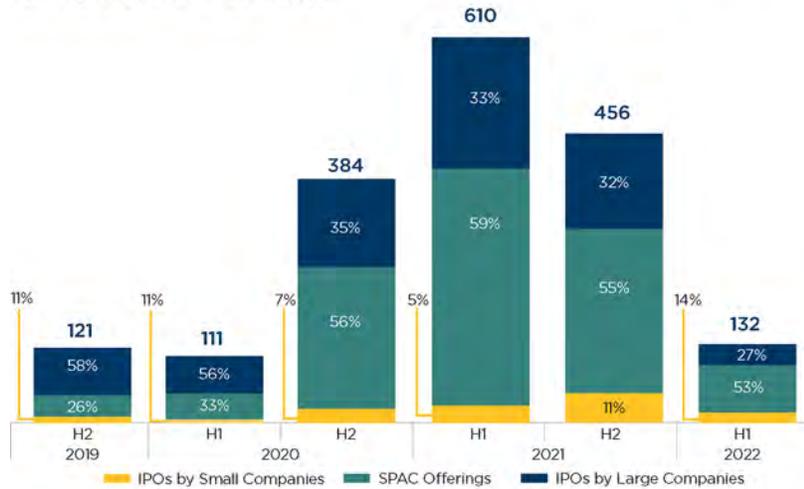


### How are the dynamics changing for companies going public?

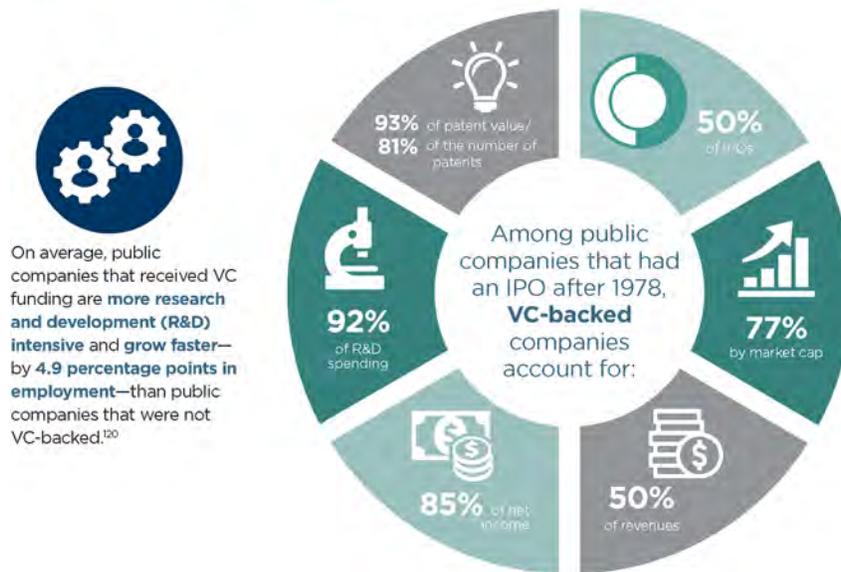
Much of the IPO market growth in 2020-2021 and decline in 2022 related to IPOs by large companies and SPAC offerings. The proceeds raised in an IPO by U.S. small companies consistently remain a **very small fraction** of the IPO market.<sup>17</sup>



The significant decline in the number of IPOs by large companies and SPAC offerings has increased how much U.S. small companies account for in the overall IPO market.<sup>118</sup>



How has venture capital affected the public markets?<sup>119</sup>



### Deeper Dive into Small Public Companies

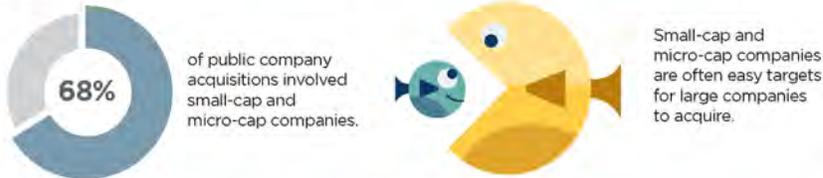
While it is easy to group all public companies together, their experiences and challenges in the public markets differ considerably. The unique challenges that small public companies face tend to receive less coverage than those faced by larger companies.

How has the number of smaller reporting companies changed since 2011?

Despite the SEC's 2018 expanded definition of smaller reporting companies (SRCs),<sup>121</sup> the number of SRCs has declined, although that number as a percentage of all reporting companies has risen slightly.<sup>122</sup>



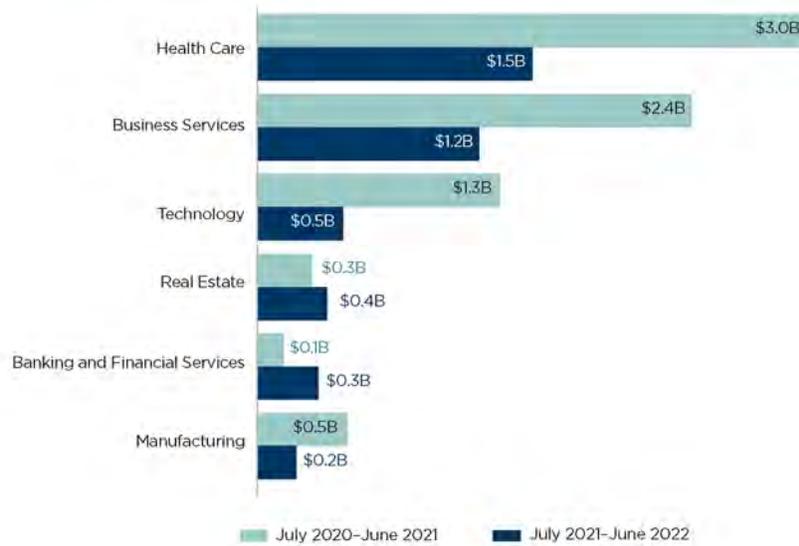
How are mergers and acquisitions affecting the number of small public companies?<sup>123</sup>



How are U.S. small public companies raising capital through registered equity offerings?<sup>124</sup>



Several industries had significant changes among equity offerings by U.S. small public companies.<sup>125</sup>



How are compliance costs affecting small public companies?

Compliance with regulatory requirements often include fixed costs that are not scalable for small public companies.<sup>126</sup> Some of those costs have disproportionately increased for smaller reporting companies.<sup>127</sup>

Average Internal Annual Sarbanes-Oxley Act Compliance Costs<sup>128</sup>

	2021	2022	Year-over-year trend	Percent change
Large accelerated filer	\$1,328,300	\$1,450,800	↑	9%
Accelerated filer (excluding SRCs)	\$1,221,900	\$1,232,400	↑	1%
Emerging growth company	\$1,408,300	\$1,370,200	↓	-3%
<b>Smaller reporting company</b>	<b>\$1,126,000</b>	<b>\$1,433,600</b>	<b>↑</b>	<b>27%</b>

The amount of research coverage and the number of analysts covering a company often correlate with a company's market capitalization.<sup>129</sup>



Small public companies are only covered by an average of two analyst firms.

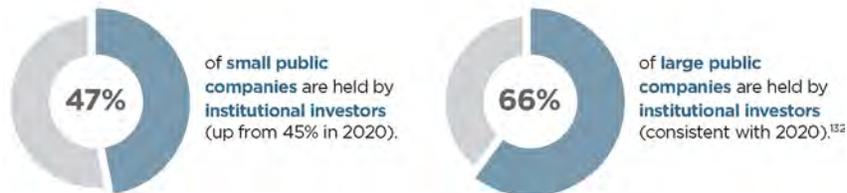


Large public companies are covered by an average of nine analyst firms.<sup>130</sup>



Less research coverage equates to additional liquidity challenges for smaller companies.

Small public companies and companies that are not able to obtain research coverage have lower levels of institutional ownership.<sup>131</sup>



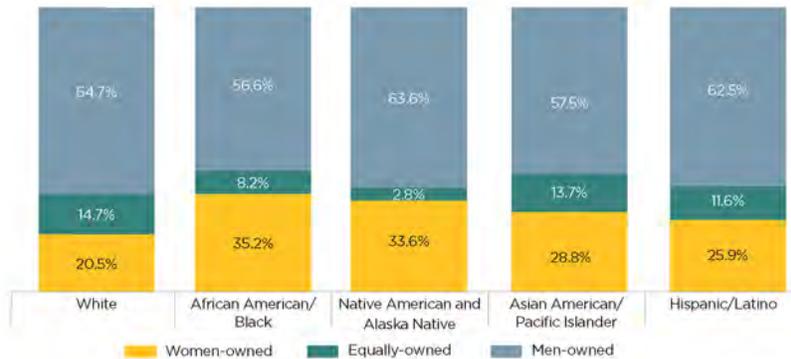
## Women Businesses Owners and Their Investors

### Women-Owned Business Formation and Ownership

The portion of businesses owned by women decreases as the businesses move through the life cycle stages.



By share of employer firms, women owners are underrepresented in every demographic group.<sup>137</sup>

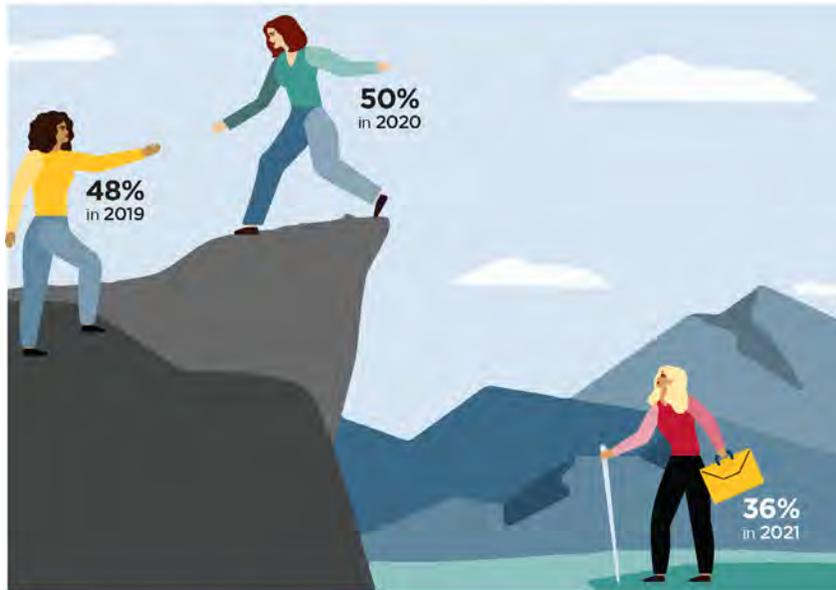


The gender gap in new entrepreneurs has been persistent over the past 25 years and continued in 2021.<sup>138</sup>

**28** out of 10,000 women became new entrepreneurs, compared to **45** out of 10,000 men.

Women founders remain resilient but feel less supported than ever.

The percentage of women founders that feel supported by the entrepreneurial community has drastically declined.<sup>139</sup>



**60%** of female founders feel held back by their gender.

**4%** of male founders feel held back by their gender.<sup>140</sup>

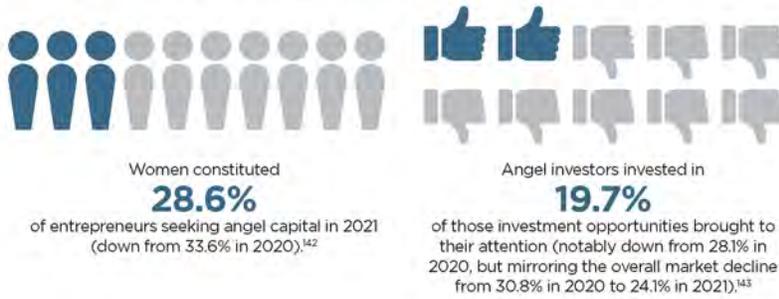
“

During the pandemic there were a number of women who left the workforce to start their own businesses—some out of necessity, some for the need of flexibility, being able to do remote work from home... what’s going to be important are the resources that support that continued growth.

TENE DOLPHIN, EXECUTIVE DIRECTOR OF THE NATIONAL WOMEN’S BUSINESS COUNCIL<sup>141</sup>

### Capital Raising Trends for Women-Owned Businesses

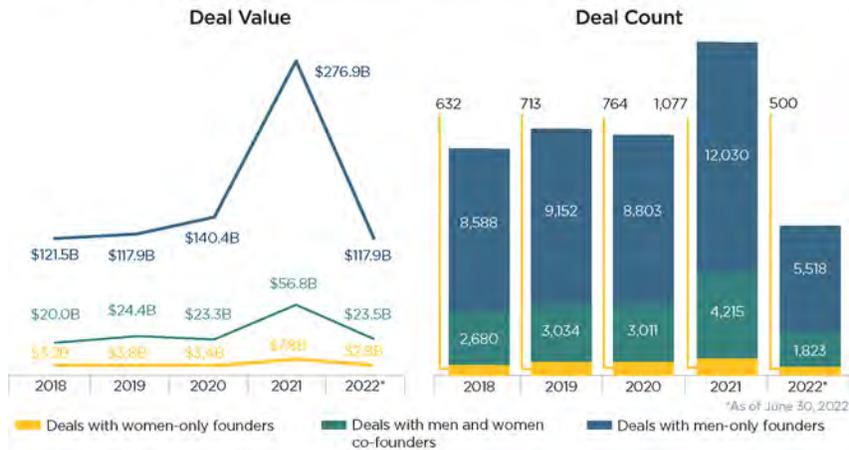
Both the number of women entrepreneurs seeking angel capital and their investment yield rate declined year over year.



While the amount of VC investment has risen significantly, the share of funding to women founders continues to lag.



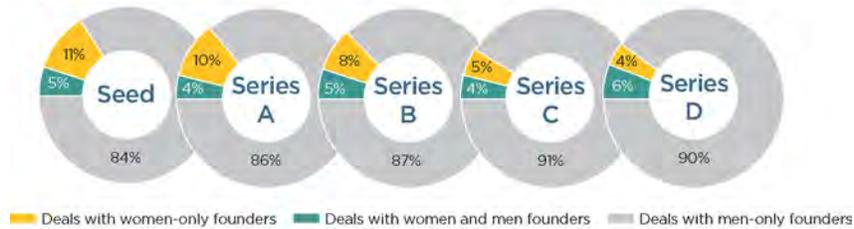
VC deal values and deal counts have trended up in recent years—peaking in 2021.<sup>146</sup>



Despite the record amount raised in 2021, women founders' share of VC funding remains a fraction of the overall capital raised.<sup>147</sup>



In 2021, women-only led teams received a declining percentage of overall invested capital in each progressive funding round.<sup>148</sup>



Some major metro areas have seen significant surges in capital raising for women founders.

Amounts raised since 2020 as a percentage of aggregate amounts raised 2008–2019.<sup>149</sup>



Despite more investor meetings for all-women teams, all-men and mixed teams continue to get more funding.<sup>150</sup>



VC investors more heavily scrutinized the team, traction, and business model in pitch decks by all-women teams, compared to all-men teams.

All-women teams experienced:<sup>152</sup>



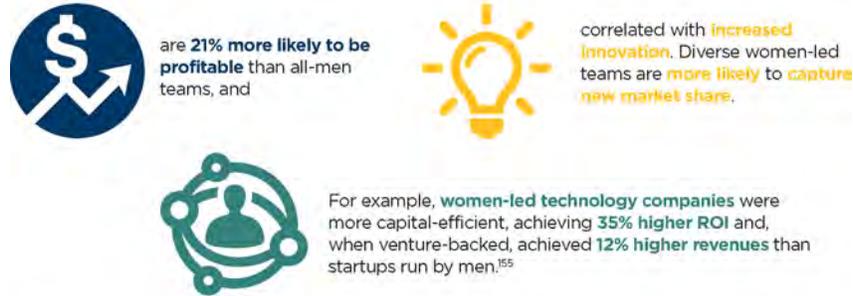
“

I hope a statistic like this prompts investors to examine their own biases more closely. For many investors, this extra scrutiny on the team slide is coming from a place of skepticism. They're wondering if a particular all-female team can really build a product and whether they have the right experience to do so. Female founders face a higher bar for questions like these, especially in male-dominated sectors.

ADRIANNA SAMANIEGO, FEMALE FOUNDERS FUND<sup>153</sup>

Executive teams with women produce better financial returns, exhibit more innovation, and outperform on time to exit.<sup>154</sup>

Executive teams with women:



2022 is on pace to be the **12th straight year** that women-founded companies are **exiting and returning capital to investors faster** than the overall market.<sup>156</sup>



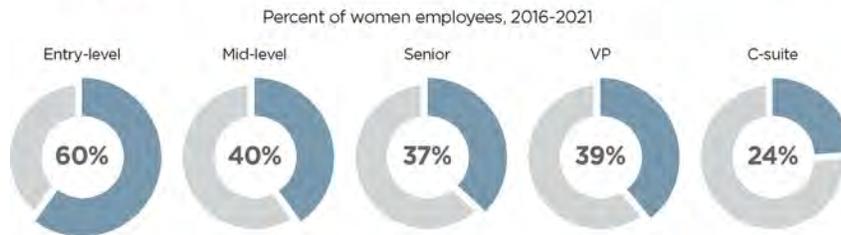
“

Firms that retain female managers by introducing policies that balance work and family, and that actively hire more female executives have superior performances than those firms that do not.

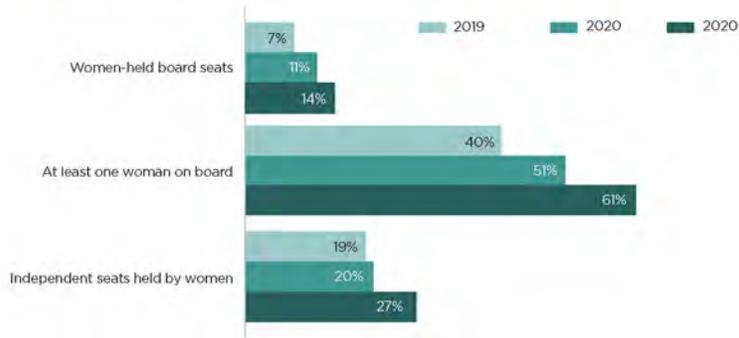
CHENGWEI LIU, ET AL.<sup>157</sup>

### Women in Leadership Roles

Women remain underrepresented in leadership roles among VC-backed companies.<sup>158</sup>



While underrepresented, the share of women in board roles at VC-backed companies continues to increase.<sup>159</sup>



Women-led IPOs increased in 2021, but remain a small share of the overall market.<sup>160</sup>



**IPOs with a woman founder or co-founder more than doubled to 48** in 2021 (up from 22 in 2020), but represented only **16%** of all public listings last year.

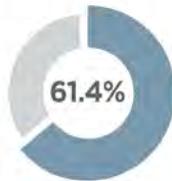
Board gender diversity among small public companies continues to improve, but progress is slowing.<sup>161</sup>



### Trends in Women Investors in Small Businesses

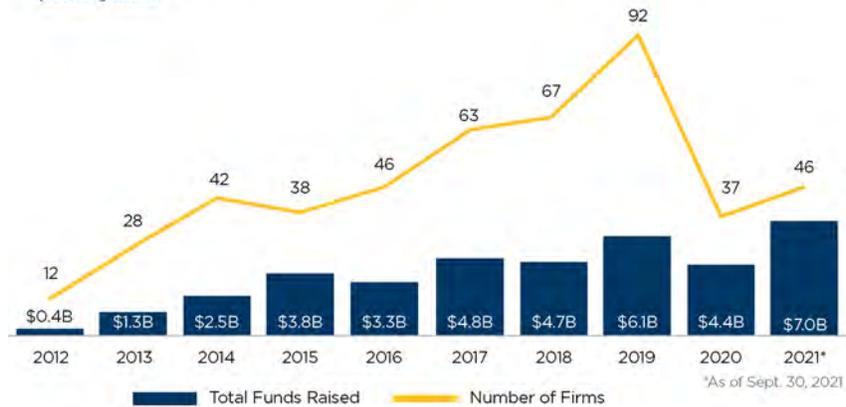
2021 was a record high for active women angel investors.<sup>162</sup>

**33.6%** of angel investors in 2021 were women (an increase from 29.5% in 2020).<sup>163</sup>



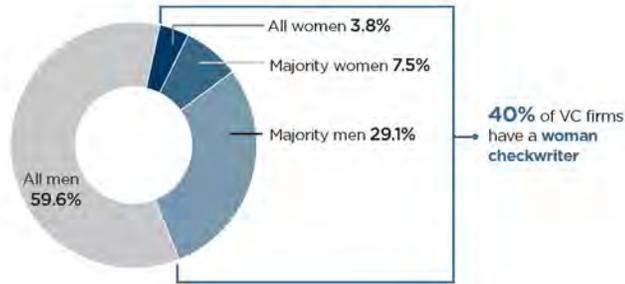
of women angel investors were active investors, compared to just 43.7% of angels in the overall market.<sup>164</sup>

Fundraising by women-founded VC and micro funds in 2021 outpaced prior years.<sup>165</sup>

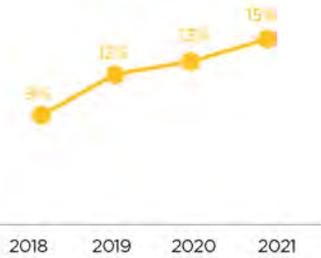


Women remain underrepresented among VC and micro fund checkwriters.<sup>166</sup>

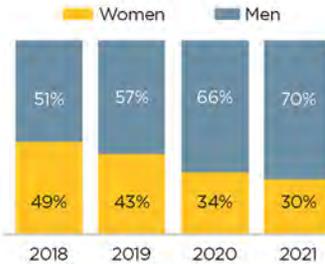
Breakdown of Checkwriters at VC Firms



Women Checkwriters



New Checkwriters



Women-led funds facilitate greater funding of diverse founders.



Women VC partners were **3X more likely to invest** in startups with **women CEOs** and often yielded superior returns.<sup>167</sup>



Promoting and recruiting **women checkwriters** can open doors for **more women founders** and **diversify portfolios**.<sup>168</sup>

“

When women and minorities are underrepresented as investment partners, our economy reaps just a fraction of the full potential that could be gained from companies founded by these communities.

IMANI AUGUSTUS, DIRECTOR OF THE ALLIANCE FOR ENTREPRENEURIAL EQUITY<sup>169</sup>

# Minority-Owned Businesses and Their Investors

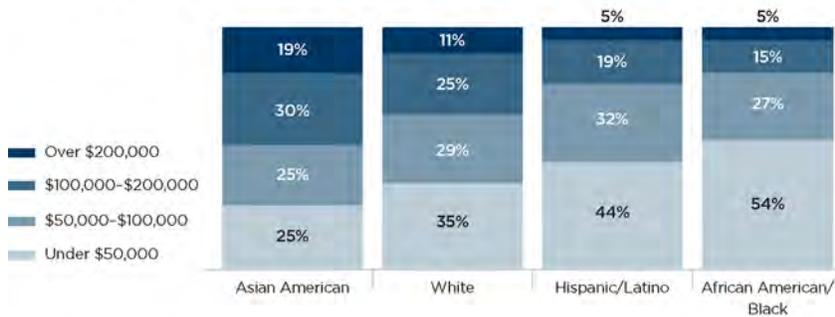
## Precursors to Accessing Capital

Inequalities across demographic groups impact the starting line for many entrepreneurs.<sup>170</sup>

Entrepreneurs who are African American/Black or Hispanic/Latino face additional barriers to entry because the increasing wealth gap affects their ability to tap personal assets as a funding source.<sup>171</sup>

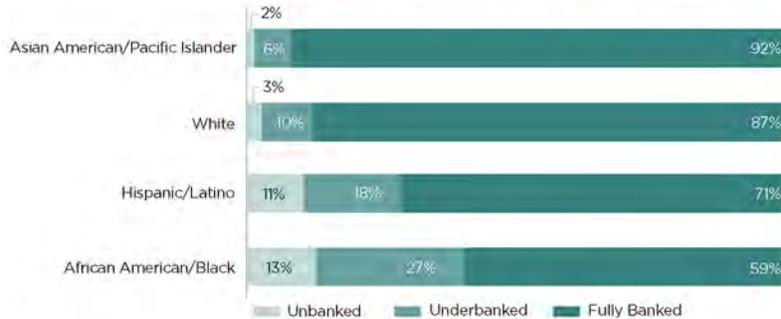


Disparities in income distribution add additional hurdles to overcome.<sup>172</sup>



Minority entrepreneurs are less likely to have access to credit.

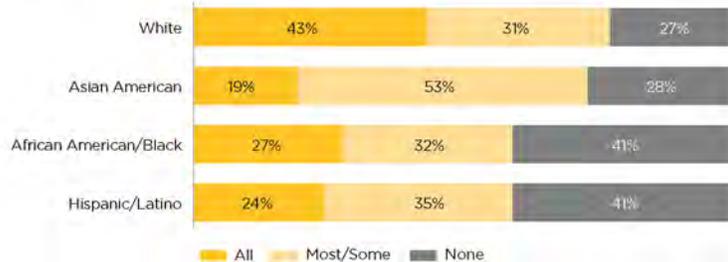
Hispanic/Latino and African American/Black households are more likely to be unbanked, meaning that no one in the household has a checking or savings account at a bank or credit union.<sup>173</sup>



Less access to traditional financial institutions means greater reliance on alternative financial services, like check cashing counters and payday lenders, which can adversely affect financial health and ability to build a credit history.<sup>174</sup> A person with limited credit history or a lower credit score is less likely to qualify for personal and business loans.

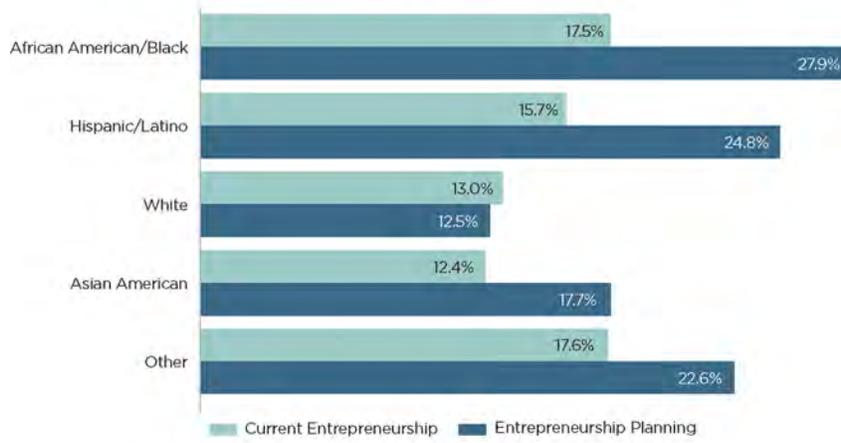


Minority entrepreneurs are less likely than White entrepreneurs to receive all the financing they seek, even when comparing applicants with similarly low-credit-risk.<sup>177</sup>



### Business Formation and Ownership Trends

Entrepreneurial activity remains high across minority groups.<sup>178</sup>



Minority entrepreneurs perceive entrepreneurship positively, but further resources are needed to support minority businesses' growth.<sup>179</sup>



African American/Black and Hispanic/Latino adults intend to **create new businesses** at **2X** the rate of White adults.



**1/3** of working age African American/Black adults are **starting or running a new business**.



White adults own **established businesses**<sup>180</sup> at almost **2X** the rate as African American/Black and Hispanic/Latino adults.



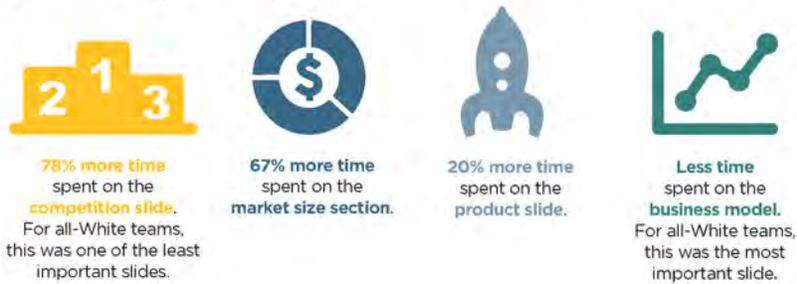
Achieving equity in entrepreneurship has the potential to unleash a new era of businesses, hiring, and generational wealth.”

MARC H. MORIAL, PRESIDENT AND CEO OF THE NATIONAL URBAN LEAGUE AND JON COWAN, PRESIDENT OF THIRD WAY<sup>181</sup>

### Capital Raising Trends

VC investors more heavily scrutinized particular deck slides of teams with minority members compared to all-White teams.

Teams with minority members experienced:<sup>182</sup>



“The discrepancies in viewing times that correlate with less funding suggest to me that investors have a harder time believing facts and statements from underrepresented founders within their pitch decks. The pre-seed round is where we’re seeing these biases emerge strongly and where founders are being overlooked the most.”

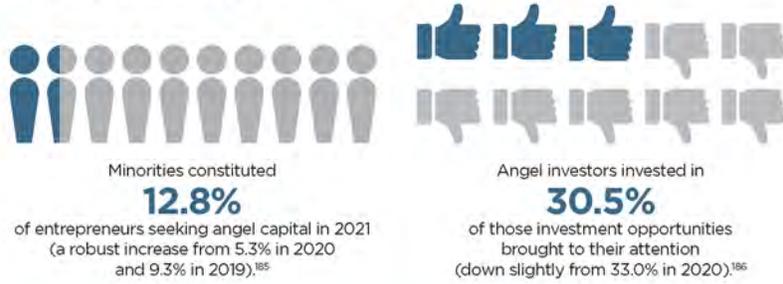
DARREL FRATER, THECLUB APP AND VISIBLE HAND VC<sup>183</sup>

At the pre-seed stage, the funding process often requires more effort and more meetings for teams with minority members.

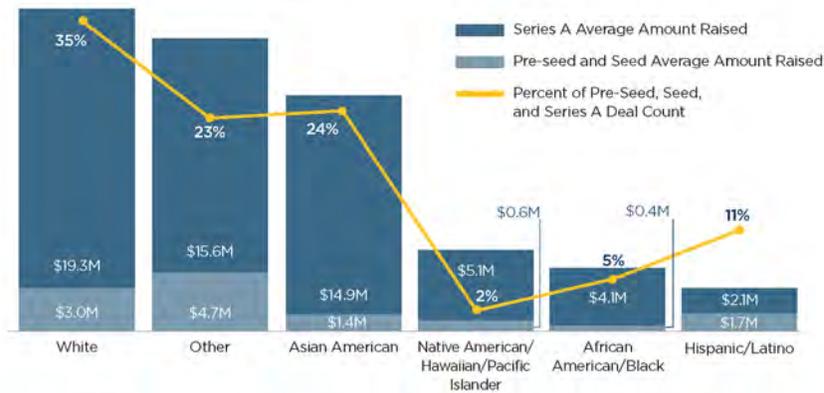
Average number of investor meetings per pre-seed fundraising:<sup>184</sup>

All-White teams			Teams with Minority Members		
All men	Women and men	All women	All men	Women and men	All women
MEETINGS	MEETINGS	MEETINGS	MEETINGS	MEETINGS	MEETINGS
37	37	35	45	71	74

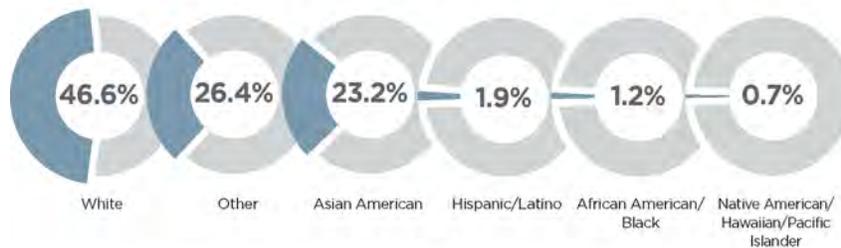
The number of minority entrepreneurs seeking angel capital is up, but underrepresentation persists.



Funding for seed and early-stage funding remains inequitably distributed as reflected in average amounts raised in 2021, broken down by race and ethnicity.<sup>187</sup>



The inequitable distribution can also be seen across the share of seed and early-stage funding in 2021, broken down by race and ethnicity.<sup>188</sup>



LGBTQ+ founders similarly report challenges accessing capital.



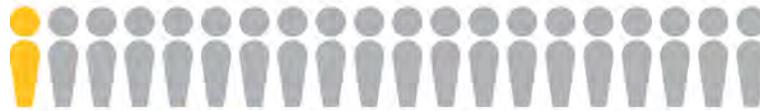
Entrepreneurs with disabilities also face obstacles accessing capital.<sup>192</sup>



“  
 A massive obstacle disabled founders face is access to capital, as is the case for all underestimated entrepreneurs. Women, Black, and Latino entrepreneurs each receive less than 3% of venture capital funding... However, when it comes to disabled entrepreneurs, the data on funding doesn't even exist.”  
 DIEGO MARISCAL, FOUNDER AND CEO OF 2GETHER-INTERNATIONAL<sup>196</sup>

### Minority Investors and Allies

Minorities among angel investors have decreased for the last three years.



**4.1%** of angel investors in 2021 were minorities (down from 5.3% in 2020 and 7% in 2019).<sup>197</sup>

Minorities remain vastly underrepresented among asset managers, but they are more likely to fund minority founders.



1.4% of the total assets under management in the U.S. are in **minority-owned funds**, but they are **3x to 4x** more likely than non-minority-owned funds to **fund minority entrepreneurs**.<sup>198</sup>

The representation of minority partners in the VC industry has remained steadily low—although the number of emerging funds launched by African American/Black partners has grown by record amounts in recent years.<sup>199</sup>

**53%** of the decision-making roles at the top U.S. VC firms are held by **White men** (down from nearly 64% of such roles in 2018).<sup>200</sup>

**27%** of African American/Black VC partners launched funds within the **past two years** barely keeping pace with the overall growth.<sup>201</sup>

**2%** of VC investment partners are Hispanic/Latino.<sup>202</sup>

**3.5X** Since 2018, the number of **African American/Black partners** who make **investment decisions and lead deals** at top U.S. VC firms **increased 3.5 times** (to over two dozen from 7).<sup>203</sup>

**59%** of Hispanic/Latino VC investment professionals work at **smaller VC funds**.<sup>204</sup>

**3X** Follow-on funds raised by **African American/Black-led** and **Hispanic/Latino-led funds** are **3X more sensitive to past performance**—with investors more harshly punishing poor performance.<sup>206</sup>

**1/2** **African American/Black-led first-time funds** were nearly **half the size of the first-time funds** raised by everyone else (averaging \$30.5 million compared to \$57 million).<sup>205</sup>

In addition to investing in minority entrepreneurs at a higher rate, minority-led VC funds can create ripple effects within the investor community.



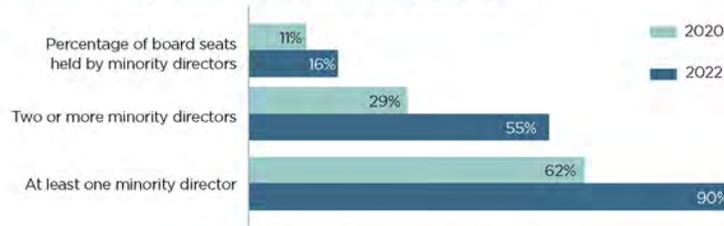
**56%** of African American/Black VC partners are actively mentoring other investors in the Black VC community.<sup>207</sup>



**25.3%** of funds that allocate part of their capital to diversity, equity and inclusion (DEI) or minority investments had a minority VC partner, compared to 5.9% of funds that don't have a DEI or minority investment allocation.<sup>208</sup>

### Public Company Board Leadership

Diversity has increased on public company boards.<sup>209</sup>



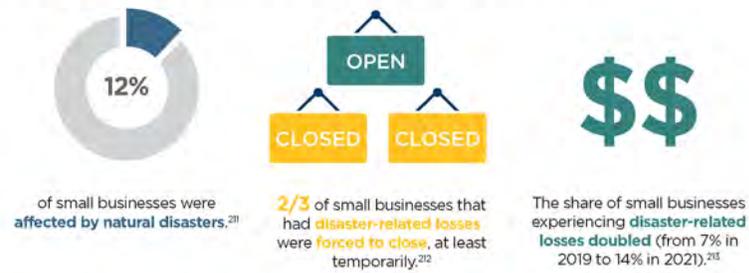
Minority representation on public company boards still lags behind the overall population.



**16%** of small public company board members in 2022 are Hispanic/Latino (3%), African American/Black (6%), or Asian American/Pacific Islander (7%), an aggregate increase from 11% in 2020.<sup>210</sup>

## Natural Disaster Areas

How do natural disasters affect small businesses?



Natural disasters affect communities and their small businesses across the country.

Between October 1, 2021 and September 30, 2022, there were 18 natural disaster events with losses exceeding \$1 billion.<sup>214</sup> The total estimated natural disaster-related losses in the U.S. exceeded \$55 billion.<sup>215</sup>



### Capital from investors remains a small portion of funding

Similar to all small and emerging businesses, those affected by natural disasters used personal funds (66%), grants and other funds that do not need to be repaid (64%), and cash reserves (57%) before seeking external capital (with repayment) (53%).<sup>216</sup> Of those that applied for external capital:

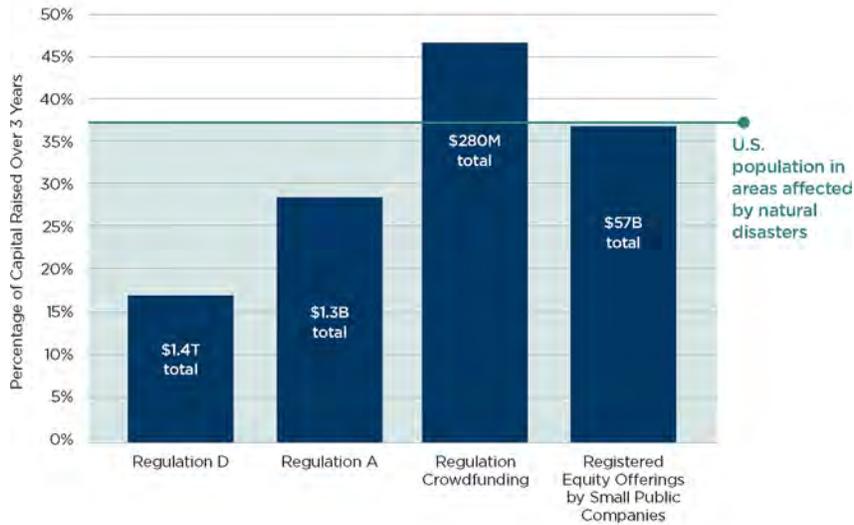
**7%** sought **equity financing** (compared to 6% of small businesses not affected).<sup>217</sup>

### How does the percentage of the population affected by natural disasters compare to the amount of capital being raised?



37% of the U.S. population<sup>218</sup> lives in an area that was affected by a natural disaster during the three years ending June 30, 2022.<sup>219</sup>

As a percentage of capital raised nationwide, capital raised by businesses in areas affected by natural disasters varied under different offering pathways.<sup>220</sup>



## Rural Communities

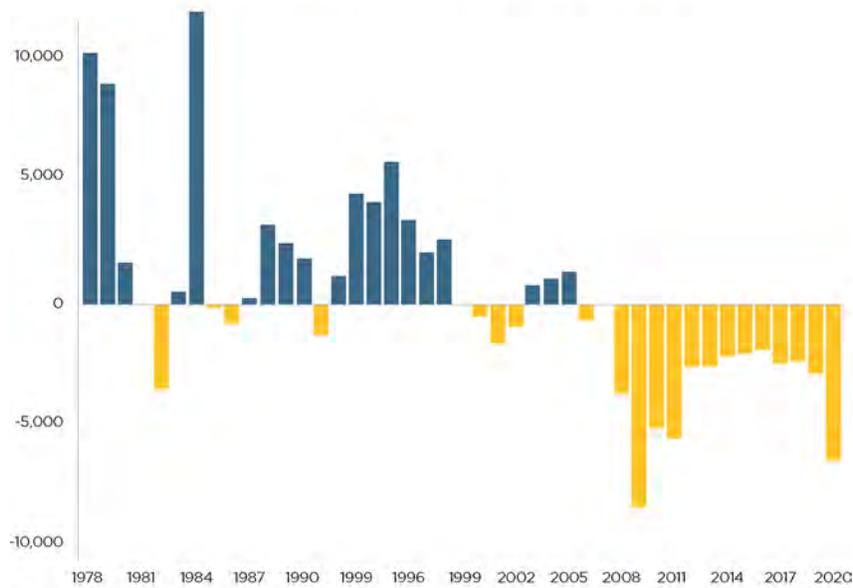
Small businesses drive employment in rural areas, despite the declining number of new small businesses

Small businesses are critical to rural communities, employing well over half of workers in rural areas.<sup>221</sup>



Since 2008, rural small business creation has fallen below the replacement level.<sup>222</sup>

Net Difference between Firm Starts and Closures in Nonmetropolitan Areas<sup>223</sup>

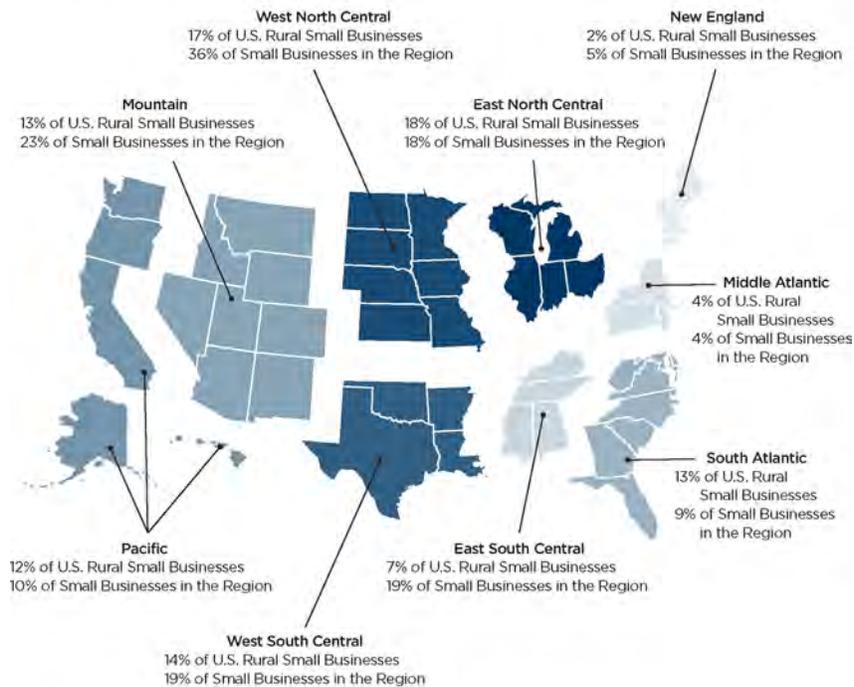




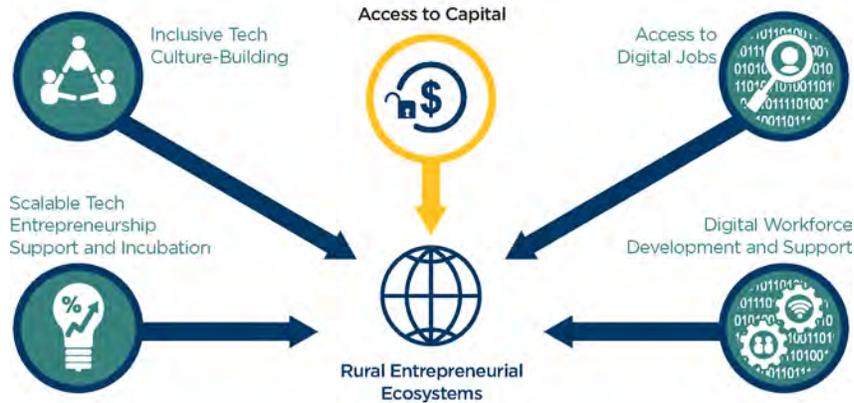
One element that is at the heart of virtually every development strategy that works well in rural communities is entrepreneurship. Every entrepreneur matters in rural communities—from the creative, home-based business, to the owner of a small Main Street business, to the larger potential growth company.”

DEB MARTIN, GREAT LAKES COMMUNITY ACTION PARTNERSHIP<sup>224</sup>

Rural small businesses are located coast to coast, with the majority in the middle of the country.<sup>225</sup> The below map illustrates the distribution of rural businesses across the U.S. by region, as well as the percentage of businesses within each region that are rural.



Access to capital is a direct driver in building rural entrepreneurial ecosystems<sup>226</sup>



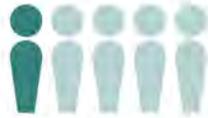
Small banks remain the primary source of capital for rural small businesses, despite the decline in small banks and small business lending



Capital from investors remains a very small portion of funding



How does the rural population compare to the amount of capital being raised?



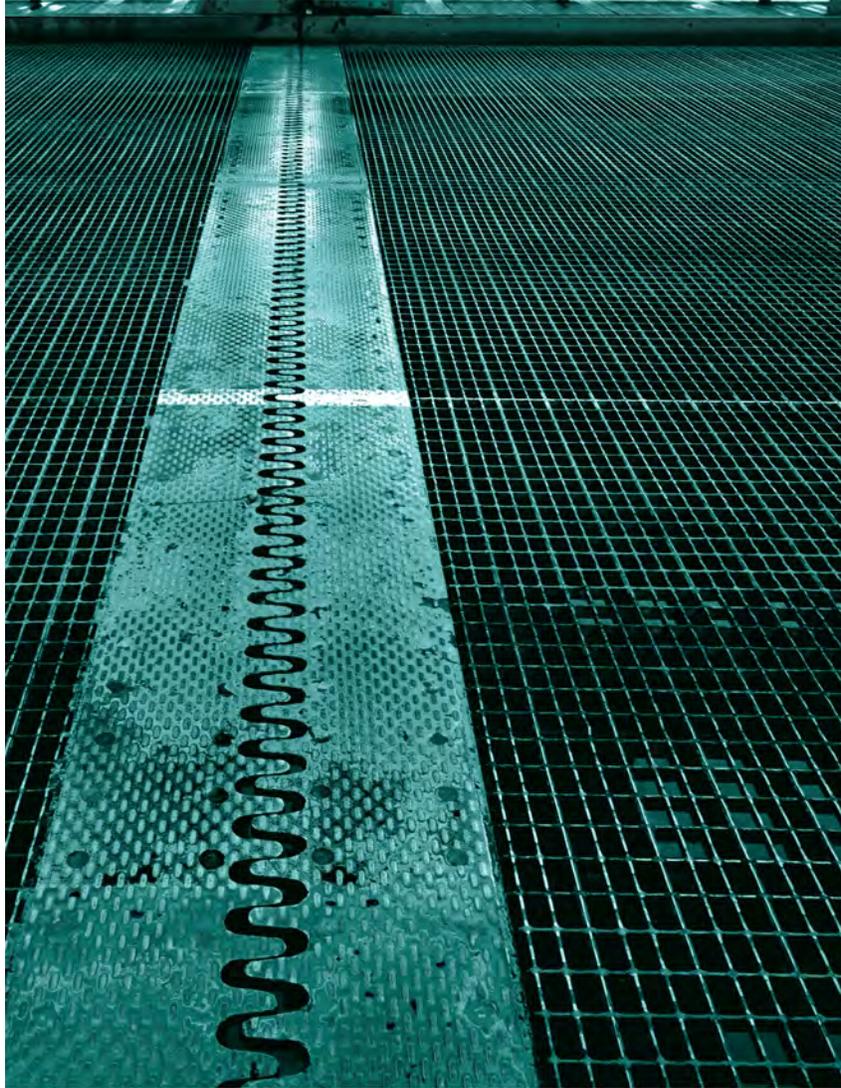
**18%**  
of the U.S. population  
lives in rural areas.<sup>231</sup>



**16%**  
of small employer firms are  
located in rural areas.<sup>232</sup>

However, businesses in rural areas<sup>233</sup> raised a notably smaller portion of overall capital relative to the rural share of population during the three years ending June 30, 2022:





## Policy Recommendations

The Office developed the following policy recommendations for Congress and the Commission based on feedback from small businesses and their investors about our capital raising rules. We have distilled their feedback into five key areas for action to address the most significant issues raised.

We recognize that for any complex issue, including challenges surrounding capital formation, there are a multitude of potential approaches, and indeed we may need to combine multiple approaches to arrive at an effective solution. For each recommendation, we include background context, particular impact on demographic groups, notes on related developments, and our proposed solution.

We welcome further engagement by Congress and the Commission to implement these solutions so that entrepreneurs and their investors together can bring innovations to market.



On August 27, 2022, our Office and the Fort Worth Regional Office joined the University of Houston C.T. Bauer College of Business for a series of discussions with entrepreneurs on their successes and challenges in starting and growing their businesses and accessing funding.

Entrepreneurs and their investors need accessible tools and educational resources to navigate complex securities laws.



### Background Context

All businesses need capital to create jobs, grow, and innovate. Many entrepreneurs need support to access that essential capital.<sup>244</sup>

Throughout the last fiscal year, we met in-person and virtually with entrepreneurs and investors from across the country. We heard countless examples of hard work and perseverance that allowed small businesses and their investors to overcome the challenges brought by the COVID-19 pandemic. We met with many founders who have been able to fund their operations using personal savings, credit cards, retained business earnings, or grants. We also talked with many small businesses owners for whom those non-dilutive funding sources were unavailable or insufficient and who were looking to investors to help finance their operations and development.

Many of the entrepreneurs we met—no matter how business savvy or technologically sophisticated—noted that the capital raising rules are complex and expressed the need for accessible resources at every stage to help them navigate the capital raising process.



### Demographic Impacts

Even as the regulatory pathways to raising capital have expanded in recent years, the complexity of our regulatory framework remains. In particular, women and minority entrepreneurs face an uneven playing field when navigating that complexity, as they do not have access to the same networks, experienced mentors and advisors, or supportive entrepreneurial communities as their counterparts.<sup>245</sup>



### Related Developments

Over the last year, the Commission has supported our partnership with other SEC offices and divisions to launch the *Capital Raising Hub*, a centralized portal of educational resources for small businesses and their investors. The *Capital Raising Hub* provides resources for each phase of the capital raising journey, and we continue to expand and update the resources based on feedback we receive through our outreach efforts.

One of the most popular resources within the *Capital Raising Hub* is our *Building Blocks* suite of educational materials, akin to “one-pagers” that break down fundamental securities law concepts into plain language. Also popular are the *Cutting through the Jargon* glossary, which demystifies common terminology, and

the Navigate your Options tool, a “choose-your-own-adventure” style resource to help users navigate through the capital raising options.



### Proposed Solution

Looking forward, we will continue to engage with diverse audiences of small businesses, investors, and other thought leaders in the market to promote and improve our educational resources. We also will continue to seek feedback and welcome suggestions for future materials.

The Commission’s continued support of our efforts in this area is critical to ensuring that entrepreneurs and their investors, at every stage, have access to tools and educational resources to understand and comply with the securities laws in order to access our capital markets effectively.



In October 2021, the Office joined Wyoming founders, investors, and other small business leaders for an engaging conversation about capital raising for early-stage companies. One participant noted the importance of accessible resources: “Entrepreneurs just want to run their business. We need to make the process simpler by using normal language that people use in their living rooms.”

## Targeted regulatory changes can improve access to capital.



### Background Context

As we engage with small businesses, investors, and other thought leaders, many share details about successes in the capital raising process as well as areas of challenges. Overwhelmingly, small businesses and investors alike tell us that Regulation D works well for businesses that have access to accredited investors.

Many small businesses across the country, however, do not have pre-existing accredited investor networks—often resulting in additional layers of challenges and hurdles when seeking to capital raise. Market participants have identified a number of targeted regulatory changes to improve the capital raising process.



"[Y]ou find that when you have a thriving capital market, you've got jobs."

ARMEER KENCHEN, SMALL BUSINESS CREDIT INITIATIVE AND  
CORNERSQUARE COMMUNITY CAPITAL<sup>269</sup>



### Demographic Impacts

Data highlighted in this report shows the dismal proportion of capital raised by small businesses founded by women and minority entrepreneurs. This is the case at all lifecycle stages—from startups through later-stage businesses seeking venture capital—leaving these businesses financially constrained and unable to reach their full potential.

Diversifying the pool of investors and capital allocators facilitates greater funding of diverse founders. Women VC partners were three times more likely than men VC partners to invest in women entrepreneurs.<sup>247</sup> Minority-owned funds were three to four times more likely than non-minority-owned funds to invest in businesses founded by minority entrepreneurs.<sup>248</sup> Therefore, policies that have a negative impact on underrepresented investors further impede investment in the next generation of diverse innovators working to grow their companies.<sup>249</sup>

For example, the accredited investor definition largely determines whether an individual is eligible to invest in many early-stage companies.<sup>240</sup> However, African American/Black and Hispanic/Latino investors are excluded from the accredited investor definition at higher rates than White and Asian American/Pacific Islander investors due, in large part, to historic wealth inequality.<sup>241</sup>

One area where data has shown progress has been [Regulation Crowdfunding](#), where women and minority founders are finding more success raising capital than through other capital raising options.<sup>242</sup>



### Related Developments

The Commission's most recent rulemaking agenda indicates that it will consider amendments to Regulation D, including updates to the accredited investor definition and Form D.<sup>243</sup>



### Proposed Solution

Based on the feedback we have received, we recommend the following changes to the accredited investor definition and Regulation Crowdfunding. We also recommend proceeding with caution on any potential changes to Regulation D or Form D.

#### ACCREDITED INVESTOR DEFINITION:

The Commission should expand the definition to include additional qualitative professional criteria and offer more opportunities to demonstrate financial sophistication as an alternative to the income and net worth thresholds.

The Commission also should consider the impact any change to the income and net worth thresholds would have on minorities and populations located in rural areas.

#### *Rationale:*

- As reflected in the data<sup>244</sup> on net worth and income inequality across demographic groups, raising the wealth thresholds would have a disparate impact on minorities, adding additional barriers to entry for minority entrepreneurs.
- In addition, increased thresholds would have a disparate impact on geographic areas with a lower cost of living, including rural areas. These regions already have less capital raising activity than urban areas.<sup>245</sup>

## REGULATION CROWDFUNDING:

The Commission or Congress should amend Regulation Crowdfunding<sup>246</sup> to increase the offering size threshold under which an issuer may meet its financial statement requirements by providing financial statements and income tax return information certified by the principal executive officer.

*Rationale:*

- Crowdfunding offerings have been a successful source of funding for many women-founded, minority-founded, and geographically diverse companies.<sup>247</sup>
- However, the requirement to have financial statements reviewed by an independent public accountant<sup>248</sup> delays the ability to commence an offering and imposes an upfront cost without a guarantee that the offering will be successful. Under the Commission's COVID-19 relief in effect from May 4, 2020 through August 28, 2022, issuers offering \$250,000 or less in a 12-month period could meet the Regulation Crowdfunding financial statement requirements by providing financial statements of the issuer and certain information from the issuer's Federal income tax returns, both certified by the principal executive officer.<sup>249</sup> The relief was available to companies that had been operating for six months or more prior to the commencement of the offering. A permanent extension of this relief would benefit small businesses that may look to meet urgent funding needs through a Regulation Crowdfunding offering.

Congress should amend Section 4A(f)(3) of the Securities Act to modify the provision that prohibits investment companies (or excluded companies under Section 3(b) or 3(c) of the Investment Company Act) from using the Regulation Crowdfunding exemption.<sup>250</sup>

*Rationale:*

- In 2020, in response to feedback, the Commission adopted Rule 3a-9 under the Investment Company Act to allow special purpose vehicles (SPVs) to conduct Regulation Crowdfunding offerings as co-issuers to a traditional issuer, provided that the SPV meets certain requirements.<sup>251</sup> Entrepreneurs and other thought leaders report that this SPV model has not worked as intended due to the prescriptive requirements and the statutory prohibition on investment companies.

**REGULATION D AND FORM D:**

When considering changes to Regulation D, we urge the Commission not to make the Form D notice and associated requirements more burdensome, particularly for small businesses.

*Rationale:*

- The Rule 506(b) safe harbor to the statutory exemption provided by Section 4(a)(2) is the most commonly used pathway to raise capital.<sup>252</sup> Any changes that deter businesses from relying on this safe harbor are likely to have a chilling effect on access to capital. In addition, such changes would be most pronounced on small businesses and those owned by women and minorities that are already facing some of the greatest challenges accessing capital.



On May 5, 2022, the Office joined National Diversity Council's Asian Love Town Hall, which focused on empowering the Asian American/Pacific Islander community and the need to bridge network gaps.

Connecting founders with savvy investors is essential to capital raising.



#### Background Context

Connecting with early-stage investors who bring relevant industry experience can have a significant and positive impact on a small business's trajectory through mentorship, business connections, strategic guidance, and follow-on financial support. Yet not all entrepreneurs have personal connections to sophisticated, early-stage investors with deep pockets and the right risk tolerance.<sup>253</sup> Registered broker-dealers tend to provide their matchmaking services for larger offerings,<sup>254</sup> but a company's need to connect with savvy investors applies regardless of the dollar-size of its offering.

Since our first Annual Report in 2019, our Office has been advocating for regulatory clarity on the role of finders in facilitating introductions between founders and investors.<sup>255</sup> This issue remains as timely today as ever.



#### Demographic Impacts

Women, minority, and rural founders often start with a smaller network of accredited, angel, and VC investors.<sup>256</sup> The lack of access to networks of potential investors has an impact that extends well beyond capital raising and into company survival and growth prospects, diversity among board leadership, and the mentoring that often comes from savvy investors. These barriers to company success in turn may affect founders' ability to build wealth and reinvest capital going forward.



Inclusive, collaborative entrepreneurial ecosystems can help bridge these long-standing gaps and dismantle... the barriers to access—opportunity, funding, knowledge, and support.... [These barriers] get in the way of too many people starting businesses and spurring economic growth.”

PHILIP GASKIN, KAUFFMAN FOUNDATION<sup>257</sup>



### Related Developments

In October 2020, the Commission proposed an order<sup>258</sup> that would permit natural persons to engage in certain limited “finders” activities involving accredited investors without registering with the Commission as brokers. The Commission has not taken further action on the proposal, and providing regulatory clarity for finders is not on the Commission’s current regulatory agenda.<sup>259</sup>



### Proposed Solution

We hear frequently that the lack of regulatory clarity on the role of finders in facilitating introductions between investors and founders harms both investors and the companies those investors are seeking to support. The lack of a clear framework makes it easier for unscrupulous intermediaries to solicit investors without disclosing hidden conflicts of interest. Further, to the extent an intermediary engages in unregistered broker-dealer activity, it could expose the company to rescission rights, which would require the company to return to investors their investment plus interest.<sup>260</sup> For decades, market participants have asked for clarity about the legal obligations of finders. We are supportive of those calls and recommend that Congress or the Commission provide additional regulatory clarity for finders.



On August 16, 2022, the Office joined a roundtable hosted by Engine where we heard about successes and challenges faced by entrepreneurs.

Emerging fund managers play a key role in small business capital formation and need support.



### Background Context

Businesses that seek funding beyond friends and family or their local angel network often turn to private funds of sophisticated pooled capital, such as VC funds. Larger funds tend to target larger investments so they can maintain a reasonably sized portfolio of companies that they can actively manage. As a result, earlier-stage, smaller deals may get pushed aside in favor of later-stage, more mature companies. Founders looking for seed and early-stage capital often struggle to raise financing for their smaller, earlier rounds. While micro-funds have strengthened seed activity, the percentage of total capital going to micro-funds and emerging fund managers remains just a sliver of the overall pie, with the percentage going to emerging fund managers declining to a new decade low.<sup>251</sup> Founders seeking smaller amounts of capital—which are typically more regional rounds—are finding less funding before the large VC funds come to the table.<sup>252</sup> For those businesses that do receive early-stage VC funding, that capital tends to be key to meeting developmental milestones, including rolling out operations, growth, and expansion.<sup>253</sup>

Emerging fund managers play a key role supporting startups across the country, particularly for those seeking smaller, early-stage financing. Their funds tend to be smaller and more likely to invest in a more diverse pool of entrepreneurs as well as businesses located in geographic areas not traditionally served by more established fund managers.<sup>254</sup> However, emerging fund managers may be disproportionately affected by the recent slowdown in IPOs, as fewer IPOs mean fewer exits resulting in distributions to a fund's LPs, which in turn may result in those LPs allocating the now smaller pool of available capital to established, larger fund managers.<sup>255</sup>



### Demographic Impacts

Diversity among those who make investment decisions results in more capital flowing to more diverse founders.<sup>256</sup>

During outreach events, we repeatedly hear that support from an institutional LP can significantly enhance a new fund's ability to attract other investors. While a number of LPs publicly pledged support for diverse fund managers following the 2020 murder of George Floyd, we hear that the amount of capital earmarked for diverse fund managers is still a tiny fraction of the total amount that institutional LPs are allocating to VC investments.<sup>257</sup>



[W]e can't believe that we're all fighting gladiator style or Hunger Games style to get a small sliver of the pie... Just because [we are] historically overlooked fund managers doesn't mean we should be looked at differently and given different opportunities for smaller slices of the pie than others.”

BRANDON BROOKS, OVERLOOKED VENTURES<sup>SM</sup>



### Related Developments

Last year, our Office recommended that Congress and the Commission explore regulatory solutions to support smaller, regional funds, including:

- Amending the “venture capital fund” definition under Rule 203(l)-1 of the Investment Advisers Act of 1940 to permit VC funds to invest in other VC funds as a “qualifying investment.”
- Improving the utility of the “qualifying venture capital fund” exemption in Section 3(c)(1) of the Investment Company Act of 1940.

The Commission has the authority to amend the “venture capital fund” definition. Congress would need to act to improve the “qualifying venture capital fund” exemption.



### Proposed Solution

Given the role that emerging fund managers play in supporting startups, we reaffirm, and expand on, the recommendations in our 2021 Annual Report. Specifically, we recommend that:

- The Commission amend the “venture capital fund” definition under Rule 203(l)-1 of the Investment Advisers Act of 1940 to treat VC funds’ investments in other VC funds to be “qualifying investments.” This would allow these investments to be excluded from the 20% non-qualifying basket.

*Rationale:*

- This amendment would allow larger—and often more geographically concentrated—funds to invest in emerging fund managers who write smaller checks, increasing both the diversity of investment decision-makers and access to capital for founders seeking smaller VC funding rounds. As noted by the SEC’s Small Business Capital Formation Advisory Committee, “larger funds tend to invest larger amounts in a handful of later-stage companies, while smaller funds tend to invest smaller amounts in a proportionate handful of earlier-stage companies. A fund-of-funds model—where a larger fund invests in smaller, regional funds—could unlock capital otherwise competing for late-stage allocations and benefit smaller companies in emerging entrepreneurial ecosystems.”<sup>269</sup>

- Congress increase the current 100 beneficial owners limit for funds that rely on the exemption in Section 3(c)(1) of the Investment Company Act of 1940.

*Rationale:*

- Limiting a fund to 100 beneficial owners can make it more difficult to raise a sufficient amount of capital. Many managers tell us that this limitation is particularly challenging for new managers who may not have the networks, track record, or access to investors who can write large checks.

- Congress increase the limit on investors in, and expand the \$10 million maximum size of, the “qualifying venture capital fund” exemption in Section 3(c)(1) of the Investment Company Act of 1940.

*Rationale:*

- As noted in our 2021 Annual Report, assuming a “2 and 20” fee structure by a fund, a \$10 million (the maximum size under the definition) qualifying venture capital fund only has \$200,000 per year to operate, inclusive of salaries, compliance, diligence, and portfolio management costs. Such a low amount sets these small funds up for failure. If Congress increases the \$10 million cap, the current 250 investor limit may impede the ability of new managers to successfully raise a sufficient amount of capital, as we have seen in the case of traditional funds relying on the exemption in Section 3(c)(1) of the Investment Company Act of 1940.

Scaled disclosures for small public companies help them stay public.



### Background Context

“Banner year for IPOs” was the headline last year. Fast forward 12 months, and we are in a very different environment. A combination of factors, including macroeconomic conditions, notably tighter monetary policy and inflationary pressures, geopolitical challenges, disruptions to supply chains, a tight labor market, the reassessment of company valuations, and recent SEC rulemakings, have contributed to the significant decline in the number of IPOs.<sup>270</sup>

Simply put, the vibrancy of our public markets depends on two key factors:

- Are private companies going public?
- Are public companies staying public?

Not only must we focus on ways to foster a robust IPO pipeline despite current macroeconomic headwinds, it is also critical that we address the challenges of staying public.



### Demographic Impacts

The demographic impacts we identify in the four recommendations above have ripple effects and are some of the leading indicators for the demographic challenges we see in the public markets. After all, a public company starts its journey as a private company and needs capital in order to mature to the point that it is ready to go public. If we are not able to address the challenges that impede women and minority founders from accessing capital to grow their startups into public companies, we are not going to see progress in the next generation of public companies led by women and/or minorities. If savvy women and minority investors do not have a role in making investment decisions, either because they do not qualify as accredited investors or because they are not able to launch or lead a fund, companies will lose out on the guidance and perspective those investors could have brought to the table. For some companies, that insight and experience could make the difference in whether they succeed in becoming and remaining a public company.

“

[D]iversity is in the interest of businesses. A diverse board helps that business be more profitable. A diverse workforce helps that business be more profitable. The value proposition of diversity is there.”

PETER HOLT, THE JOINT CORPORATION<sup>271</sup>



### Related Developments

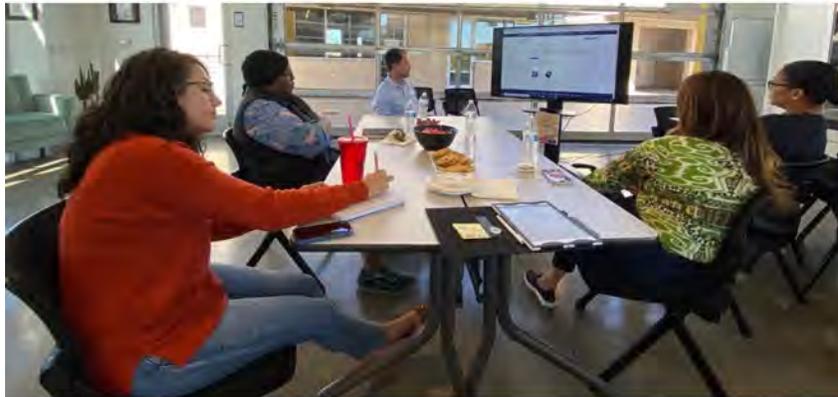
The vibrancy of our capital markets depends on having companies of varying sizes. Last year, we recommended tailoring the SEC's disclosure and reporting framework to the complexity and size of operations of companies. In particular, we highlighted the need for scaling disclosure obligations or delaying compliance for small public companies.

Since then, the Commission has embarked on a number of initiatives that will affect the disclosures that public companies make. In some cases, the Commission has taken steps to scale obligations or delay compliance for small public companies,<sup>272</sup> and in other cases, small public companies will be subject to the same requirements at the same time as much larger companies.<sup>273</sup>



### Proposed Solution

Small public companies, compared to larger ones, receive less research coverage, attract lower levels of institutional investors, and are more sensitive to fixed compliance costs.<sup>274</sup> It is imperative that we create an environment that nurtures and supports those small public companies staying public. Absent this, we will continue to see a declining number of small public companies,<sup>275</sup> which translates into fewer investment choices for investors.



On March 17, 2022, our Office met with women entrepreneurs in Phoenix, AZ where we heard about challenges they face raising capital.

With this in mind, we recommend that the Commission, when considering new disclosure obligations for public companies, scale those obligations and delay compliance for small public companies. Scaling disclosure obligations helps to better balance the costs and benefits of the rules, particularly because the proportional expense of costs that are not scalable is higher for small public companies. Delaying compliance for small public companies helps to promote better initial disclosure for those companies, as they will benefit from seeing the disclosure that large public companies prepare in response to similar new requirements.



[R]ules and exceptions out there for small reporting companies and emerging growth companies—that is really pivotal to what allowed SkyWater to become a public company when we did. Without that, we very likely would not have been able to capitalize on the opportunity to go to market and become a public company in 2021.”

STEVE MANKO, SKYWATER TECHNOLOGY, INC.<sup>278</sup>



## Small Business Capital Formation Advisory Committee FY2022 Summary

The Small Business Advocate Act also established the SEC's Small Business Capital Formation Advisory Committee. The Committee is designed to provide a formal mechanism for the Commission to receive advice and recommendations on Commission rules, regulations, and policy matters affecting; small businesses, from emerging, privately-held companies to publicly-traded companies with less than \$250 million in public market capitalization; trading in securities of such companies; and public reporting and corporate governance of such companies. The Office provides administrative support for the Committee, which otherwise functions independently.

The Committee's membership includes company and investor representatives, and other thought leaders from across a diverse set of experiences, industries, geographies, and company life cycle stages. The Commission is grateful for their service and commitment to small businesses and their investors.

The members of the Committee as of the end of fiscal year 2022 were as follows:



CARLA GARRETT, *Chair*  
Corporate Partner,  
Potomac Law Group PLLC  
Washington, DC



YOUNGRO LEE,  
*Assistant Secretary*  
CEO and Co-Founder,  
NextSeed  
Houston, TX



JEFFREY M. SOLOMON,  
*Vice Chair*  
Chief Executive Officer,  
Cowen, Inc.  
New York, NY



DONNEL BAIRD  
Founder and CEO,  
BlocPower LLC  
Brooklyn, NY



GREGORY YADLEY, *Secretary*  
Partner, Shumaker,  
Loop & Kendrick, LLP  
Tampa, FL



WILLIAM M. BEATTY\*  
Securities Administrator of the  
Washington State Securities  
Division  
Olympia, WA



**KESHA CASH**  
 Founder and General Partner,  
 Impact America Fund  
*Oakland, CA*



**GREG DEAN\***  
 Senior Vice President of the Office  
 of Government Affairs, FINRA  
*Washington, DC*



**BAILEY DEVRIES\***  
 Associate Administrator for the  
 Office of Investment & Innovation,  
 U.S Small Business Administration  
*Washington, DC*



**ROBERT FOX**  
 National Managing Partner,  
 Professional Standards Group,  
 Grant Thornton LLP  
*Chicago, IL*



**STEPHEN GRAHAM**  
 Co-Chair, Fenwick & West LLP's  
 Life Sciences Practice  
*Seattle, WA*



**SARA HANKS**  
 CEO and Co-Founder,  
 CrowdCheck, Inc.  
*Alexandria, VA*



**BRIAN LEVEY**  
 Chief Business Affairs and Legal  
 Officer, Upwork Inc.  
*San Francisco, CA*



**SAPNA MEHTA**  
 General Counsel & Chief  
 Compliance Officer, Rise of  
 the Rest Seed Fund; Associate  
 General Counsel, Revolution  
*Washington, DC*



**CATHERINE MOTT**  
 Founder and CEO of  
 BlueTreeCapital Group,  
 BlueTree Allied Angels, and  
 BlueTree Venture Fund  
*Pittsburgh, PA*



**JASON SEATS**  
 Chief Investment Officer,  
 Techstars  
*Austin, TX*



**MARC OORLOFF SHARMA\***  
 Chief Counsel of the Office of the  
 Investor Advocate, U.S. Securities  
 & Exchange Commission  
*Washington, DC*



**HANK TORBERT**  
 President, AltaMax, LLC  
*New Orleans, LA*



**SUE WASHER**  
 President and CEO, Applied  
 Genetic Technologies Corporation  
*Gainesville, FL*

\* Committee members include the SEC's Advocate for Small Business Capital Formation (vacant at the end of fiscal year 2022) and three non-voting members appointed by each of the SEC's Investor Advocate, the North American Securities Administrators Association (NASAA), and the Small Business Administration, as well as an observer appointed by the Financial Industry Regulatory Authority (FINRA).

### Summary of Activities

The Committee met virtually four times during FY2022. Materials from the meetings, including agendas, transcripts, webcasts, and presentations, are available on the Committee's webpage.

Meeting Date	Agenda Topics
<b>November 16, 2021</b>	Rural Entrepreneurship and the Challenges Accessing Financial Capital and the U.S. Department of Treasury's State Small Business Credit Initiative
<b>February 10, 2022</b>	Accredited Investor Definition
<b>May 6, 2022</b>	Proposed Rules on Climate-Related Disclosures and SPACs, Shell Companies, and Projections
<b>August 2, 2022</b>	Secondary Market Liquidity for Investors in Regulation A and Regulation Crowdfunding Companies and Smaller Public Companies



## Committee Recommendations

During fiscal year 2022, the Committee put forward the following four recommendations to the Commission:

### Accredited Investor Definition

February 10, 2022

According to the Commission's [rulemaking agenda](#), the Division of Corporation Finance is considering recommending that the Commission seek public comment on updates to the financial thresholds in the definition of "accredited investor" as set forth in Securities Act Rule 501(a) of Regulation D. The definition was most recently amended in 2020, and in connection with that rulemaking, the Committee made [several recommendations in 2019](#).

The Committee recognizes the complexity of crafting a workable definition of accredited investor that balances protecting investors with facilitating capital formation and investment opportunities. As the Commission considers updating the definition's financial thresholds for individual investors' net worth and annual income, the Committee urges the Commission to avoid unintended consequences. It is also important for the Commission to recognize that a business's failure to succeed is not the same thing as fraud. And further, fraud occurs at the hands of bad actors regardless of regulatory thresholds. The Committee believes that the SEC should continue its robust enforcement program to root out fraud across markets of all sizes, while supporting investor education on the importance of portfolio diversification to mitigate risk of one investment's failure.

Accredited investors are a critical source of early-stage capital for small businesses in communities across the country, and changes that would shrink the pool of currently accredited investors would have a detrimental effect on small business capital formation. The ripple effects of limiting access to early-stage capital would negatively impact access to future rounds of financing from funds and other later-stage investors, rippling further into the companies that will one day go public.

The Committee is also concerned that raising the thresholds could have disproportionate impacts on various demographic groups, making the definition less inclusive and widening the nation's already wide racial wealth gap. The Committee discussed the wealth gap among different racial and ethnic groups, as well across different geographic communities. The Commission should be mindful of the disparate impacts that increases to the financial thresholds could have on the pool of accredited investors. A more homogeneous pool of accredited investors would negatively impact the diversity of entrepreneurs who raise capital, decreasing inclusion in capital formation.

Further, the Committee discussed the additional ripple effects that raised financial thresholds would have on companies whose shareholders may no longer qualify as accredited investors, inadvertently triggering the registration thresholds of Section 12(g).

In light of the foregoing and consistent with the Committee's 2019 recommendations, the Committee presents the following new recommendations to the Commission for consideration in connection with potential future rulemaking on the definition of accredited investor:

1. Do not increase the current financial thresholds for individual investors to qualify as accredited.
2. Going forward, consider indexing the financial thresholds for inflation on a periodic basis.
3. Given the imperfect proxy that financial thresholds provide for measuring investor sophistication, provide alternative methods for investors to qualify as sophisticated, which could include investment experience, knowledge gained through work experience or membership in associations, education credentials, additional professional certifications, or tests to demonstrate sophistication.

Lastly, given the impact of early-stage investors who tend to invest within their local communities, as well as regional differences in income and wealth, the Committee recommends that the Commission consider creating a new exemption for local and/or micro-investments that would not be limited to accredited investors.

## Climate-Related Disclosures Proposal

May 6, 2022

On March 21, 2022, the Commission proposed rules on the [Enhancement and Standardization of Climate-Related Disclosures for Investors](#) (Release No. 33-11042). As the Commission works toward finalizing the proposed rules, while the Committee recognizes that climate is an important topic, the Committee urges the Commission to consider:

- Providing a more detailed cost-benefit analysis, including the impact that the proposed rules would have on smaller public and private companies;

- Scaling and delaying the compliance requirement for emerging growth companies, along with smaller reporting companies;
- Expanding the safe harbor for liability for Scope 3 emissions disclosures to include all climate-related disclosures;
- Eliminating the attestation requirement, as it would be costly and burdensome, and it will delay reporting;
- Requiring the information to be furnished, rather than filed;
- Tailoring the requirements for certain industries;
- Re-evaluating the timing for filing climate-related disclosures since the information may not be available in time for a company's annual report on Form 10-K; and
- Providing a longer implementation timeframe for the new rules, so that smaller companies would have more time to transition, work through implementation, and comply with the new requirements.

In addition, the Committee has the following observations and suggestions:

1. The Committee asks that the Commission consider incentives, rather than penalties, for companies that are providing climate-related disclosures. Companies that are moving in the direction of doing things that are more climate-friendly may, for instance, be deterred from putting together an analysis due to concerns of having to disclose it before it is finalized or concerns of being required to provide additional disclosures that could be financially costly and time-consuming.
2. The Committee urges the Commission consider how the climate-related disclosure requirements may deter private companies from going public. There should be a pathway for very small companies to become public reporting companies without hiring expensive climate-related consultants.
3. The Commission should consider the rule's impact on small companies that are suppliers or vendors for public companies. To the extent public companies are required to track and provide downstream greenhouse gas emissions, smaller suppliers and vendors that are unable or delayed in providing their greenhouse gas emissions may lose business to larger companies that can provide such metrics. Due to disadvantages arising from lack of resources and smaller operations scale, both small public and private companies may face greater challenges in accessing capital and generating revenue they need to sustain their businesses.

## SPACs Proposal

May 6, 2022

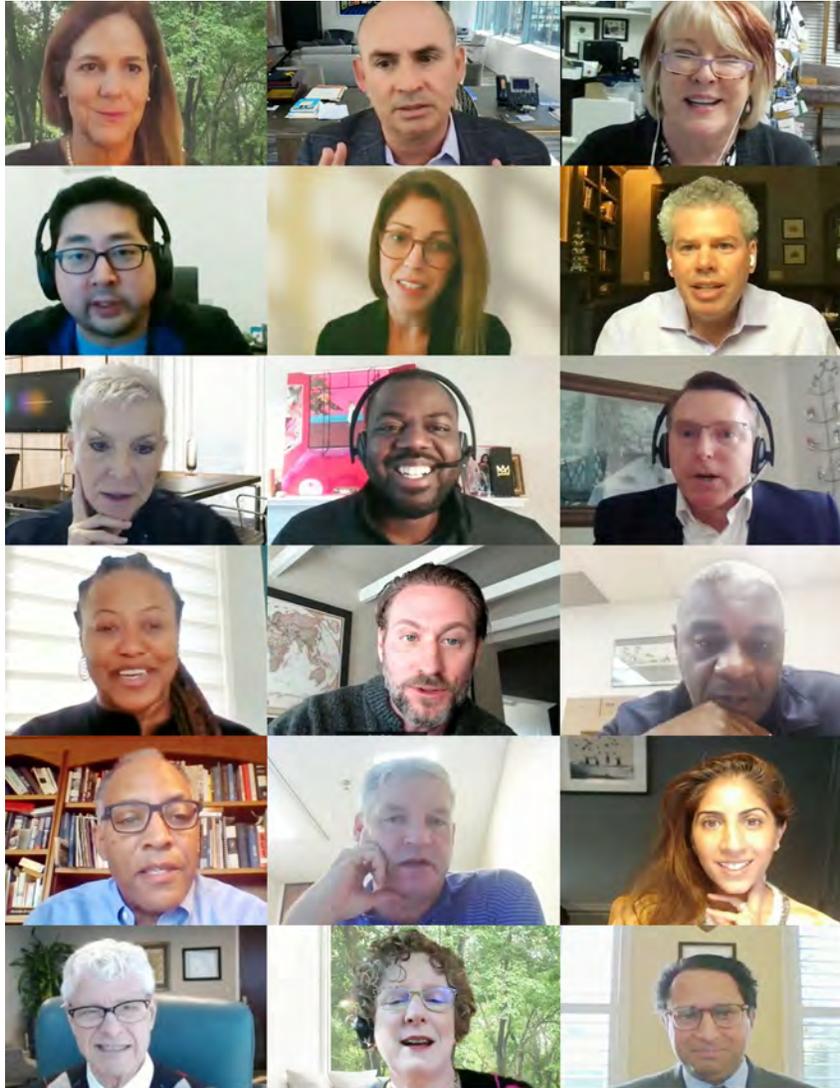
On March 30, 2022, the Commission proposed rules on [Special Purpose Acquisition Companies \(SPACs\)](#), [Shell Companies and Projections](#) (Release No. 33-11048). The Committee's recommendations related to this proposal are as follows:

1. The Committee would like for SPACs to remain a viable path for companies to pursue as a means of getting access to public market capital. The Committee is concerned that the proposed rules, as written, might render SPACs unusable as an alternative to IPOs.
2. The Committee is generally supportive of improving disclosures for SPACs, particularly in the period of time between the announcement of the merger and the closing of the de-SPAC transaction.
3. The Committee encourages the Commission to clearly identify which participants would have underwriter liability. Participants should be held accountable to the same extent they would be in traditional IPOs.
4. Management projections are an important part of the rationale for companies in determining whether to engage in a merger with a SPAC, and they are necessary when financial intermediaries provide fairness opinions related to de-SPAC transactions. As a result, the Committee recommends that the projections in de-SPAC transactions be covered by the liability safe harbor provisions of the Private Securities Litigation Reform Act when disclosed in the de-SPAC transaction.
5. The Committee recommends that the Commission expand or eliminate the 18 month and 24 month timelines provided in the Investment Company Act safe harbor for SPACs. The requirement to engage in a de-SPAC transaction within 18 months after its IPO and complete its de-SPAC transaction within 24 months could incentivize SPAC sponsors to engage in riskier acquisitions to complete the merger process within the artificially short periods.

## Regulation A Secondary Market Liquidity

August 2, 2022

The Committee discussed secondary market liquidity issues. Provided that statutory authority can be established, the Committee recommends that the Commission, on a pilot basis, provide federal preemption from state regulation for secondary sales by investors of securities initially sold pursuant to Tier 2 of Regulation A. This recommendation is limited to issuers current in their ongoing reports and whose primary offering was subject to Staff review.



## Endnotes

- 1 The SEC conducts the Forum annually and prepares a report in accordance with the Small Business Investment Incentive Act of 1980 [15 U.S.C. 80c-1 (codifying section 503 of Pub. L. No. 96-477, 94 Stat. 2275 (1980))].
- 2 See <https://www.sec.gov/education/capitalraising>
- 3 This graphic is based on DERA data. This graphic depicts amounts reported or estimated as raised from July 1, 2021 through June 30, 2022. Data on offerings under Regulations D and Crowdfunding is based on information reported by companies and was collected from EDGAR filings (new filings and amendments) on Forms D and C, respectively. Data on registered offerings was collected from Thomson Financial's SDC Platinum database. For offerings under Regulation Crowdfunding, except where specified otherwise, estimates of the number of offerings are based on offerings completed during this period as shown on progress updates on Form C-U; estimates of amounts raised are based on proceeds reported in progress updates filed on Form C-U during the report period. For offerings under Regulation A, except where specified otherwise, estimates of the number of offerings are based on offerings qualified during this period, excluding post-qualification amendments; estimates of amounts raised are based on proceeds reported in filings made during the report period. Capital raised is based on information reported by companies in Forms 1-Z, 1-K, 1-SA, 1-U, and offering circular supplements pertaining to completed and ongoing Regulation A offerings and post-qualification amendments, and for companies whose shares have become exchange-listed, information from other public sources. Estimates represent a lower bound on the amounts raised given the timeframes for reporting proceeds following completed or terminated offerings and that offerings qualified during the report period may be ongoing. For the offerings that permit pooled investment funds, such as Rule 506(b) and (c) of Regulation D and registered offerings, the data includes offerings conducted by pooled investment funds.
- 4 "Other exempt offerings" includes estimated amounts raised under Regulation S, and Rule 144A for calendar year 2021. The data used to estimate the amounts raised in 2021 for other exempt offerings includes: (1) offerings under Regulation S that were collected from Thomson Financial's SDC Platinum service; and (2) resale offerings under Rule 144A that were collected from Thomson Financial's SDC New Issues database, the Mergent database, and the Asset-Backed Alert and Commercial Mortgage Alert publications, to further estimate the exempt offerings under Regulation S. We include amounts sold in Rule 144A resale offerings because those securities are typically issued initially in a transaction under Section 4(a)(2) or Regulation S but generally are not included in the Regulation S data identified above. These numbers are accurate only to the extent that these databases are able to collect such information and may understate the actual amount of capital raised under these offerings if issuers and underwriters do not make this data available. The data on Rule 144A debt offerings from Mergent is available only through September 30, 2021. We have extrapolated the data to obtain a full calendar year. We do not yet have data to provide an estimated amount raised under Regulation S and Rule 144A for the 12 month period ended June 30, 2022.
- 5 17 C.F.R. § 230.506(b); see <https://www.sec.gov/smallbusiness/exemptofferings/rule506b>.
- 6 17 C.F.R. § 230.506(c); see <https://www.sec.gov/smallbusiness/exemptofferings/rule506c>.
- 7 17 C.F.R. § 230.504; see <https://www.sec.gov/smallbusiness/exemptofferings/rule504>.
- 8 17 C.F.R. § 227.100 et seq.; see <https://www.sec.gov/smallbusiness/exemptofferings/regcrowdfunding>.
- 9 Securities Act of 1933 § 3(a)(11), 17 C.F.R. § 230.147, and 17 C.F.R. § 230.147A; see <https://www.sec.gov/smallbusiness/exemptofferings/intrastateofferings>.
- 10 17 C.F.R. § 230.251 et seq.; see <https://www.sec.gov/smallbusiness/exemptofferings/rega>.
- 11 See <https://www.sec.gov/investor/alerts/ipo-investorbulletin.pdf> for more information.
- 12 15 U.S.C. § 77a, et seq.; see <https://www.sec.gov/smallbusiness/goingpublic>.

- 13 This graphic presents capital raised in registered, Regulation D and Regulation A offerings across the top industries from July 1, 2021 through June 30, 2022. Offerings by non-pooled investment funds in other industries accounted for approximately \$2.5 billion, \$79 billion and \$96 million in registered, Regulation D and Regulation A offerings, respectively. Regulation A and registered offerings were classified into industry groups based on the primary SIC code reported by the company. Industry groups were self-reported by companies on Form D. Differences in data sources and definitions may limit the comparability of industry data. Offerings by pooled investment funds, which accounted for approximately \$63 billion and \$2.1 trillion in registered offerings and Regulation D, respectively, are excluded from this graphic. See *supra* note 3 for a description of how these amounts were reported or estimated.
- 14 The maps included in this section depict the amounts reported or estimated as raised by issuers, including pooled investment funds that report a primary location in the U.S., including U.S. territories, from July 1, 2021 through June 30, 2022. See *supra* note 3 for a description of how these amounts were reported or estimated.
- 15 See Crowdfund Capital Advisors, “Investment Crowdfunding, Democratizing Access to Capital. 2021 Annual Report, “Feb. 2022” at 9, 12-13, 31-32 and 49, available at <https://crowdfundcapitaladvisors.com/2021-investment-crowdfunding-year-in-review-report-released/>.
- 16 Because of lags in offering qualifications, withdrawals, and abandonments, for greater comparability, this analysis considers all initiated Regulation Crowdfunding offerings and does not exclude offerings that are subsequently withdrawn or abandoned. See *supra* note 3 for a description of how these amounts were reported or estimated.
- 17 Because of lags in offering qualifications, withdrawals, and abandonments, for greater comparability, this analysis considers all initiated Regulation Crowdfunding offerings and does not exclude offerings that are subsequently withdrawn or abandoned. See *supra* note 3 for a description of the methodology used to calculate this data. Effective March 15, 2021, the maximum aggregate amount that an issuer is permitted to raise under Regulation Crowdfunding in a 12-month period was raised to \$5 million (from \$1.07 million). See “Facilitating Capital Formation and Expanding Investment Opportunities by Improving Access to Capital in Private Markets,” (Mar. 10, 2021) available at <https://www.sec.gov/corpfin/facilitating-capital-formation-secg>.
- 18 See *supra* note 3 for a description of the methodology used to calculate this data. Effective March 15, 2021, the maximum aggregate amount that an issuer is permitted to raise under Rule 504 of Regulation D in a 12-month period was raised to \$10 million (from \$5 million). See Facilitating Capital Formation and Expanding Investment Opportunities by Improving Access to Capital in Private Markets, *supra* note 17. Offerings under Rule 504 accounted for 0.9% of all new Regulation D offerings and 0.03% of the aggregate amounts raised under Regulation D. From March 15, 2021 through June 30, 2022, there were 12 offerings that raised between \$5 and \$10 million under Rule 504 for an aggregate of \$77.6 million.
- 19 This graphic includes the top industries based on the reported amounts raised by non-pooled fund issuers during the respective periods. Offerings by non-pooled fund issuers in other industries accounted for approximately \$62 billion and \$86 billion in the twelve months ended June 30, 2021 and 2022, respectively. See *supra* note 3 for a description of the methodology used to calculate this data.

- 20 Because of lags in offering qualifications, withdrawals, and abandonments, for greater comparability, this analysis considers all initiated Regulation A offerings (whether qualified or not) and does not exclude offerings that are subsequently withdrawn or abandoned. Due to lags and bunching in proceeds data and temporary relief provided to Regulation A in March 2020, the dollar amounts in this graphic are based on the amounts sought (in \$ million) in qualified Regulation A offerings and not on reported proceeds. See *supra* note 3 for a description of the methodology used to calculate this data. Effective March 15, 2021, the maximum aggregate amount that an issuer was permitted to raise under Tier 2 of Regulation A in a 12-month period was raised to \$75 million (from \$50 million). See Facilitating Capital Formation and Expanding Investment Opportunities by Improving Access to Capital in Private Markets, *supra* note 17.
- 21 This graphic includes the top industries by aggregate amounts sought in qualified Regulation A offerings during the respective periods. Additional offerings accounted for approximately \$81 million and \$162 million in the twelve months ended June 30, 2021 and 2022, respectively. See *supra* note 3 for a description of the methodology used to calculate this data.
- 22 This graphic includes pooled funds. See *supra* note 3 for a description of the methodology used to calculate this data.
- 23 This graphic includes the top industries by IPO proceeds. Additional IPOs by non-pooled fund issuers accounted for approximately \$9.6 billion and \$7.6 billion in the twelve months ended June 30, 2021 and 2022, respectively. Pooled investment funds, including SPACs, accounted for approximately \$179 billion and \$60 billion in the twelve months ended June 30, 2021 and 2022, respectively. See *supra* note 3 for a description of the methodology used to calculate this data.
- 24 See NVCA, “2022 Yearbook,” (Mar. 2022) at 10 (noting that VCs typically invest in young, high-growth companies in need of capital to grow) available at <https://nvca.org/wp-content/uploads/2022/03/NVCA-2022-Yearbook-Final.pdf>. See also Thomas Huckabee, “Not All Startups Are a Fit for the VC Funding Model: Why They Need Projected Revenues of over \$25 Million,” *Thomas Huckabee, Inc.*, (June 11, 2021) available at <https://tehepa.net/uncategorized/not-all-startups-are-a-fit-for-the-vc-funding-model-why-they-need-projected-revenues-of-over-25-million/>.
- 25 See Daniel Wilmoth, Ph.D., “Small Business Facts. Small Business Job Creation,” *U.S. Small Business Administration Office of Advocacy*, (Apr. 2022) available at <https://cdn.advocacy.sba.gov/wp-content/uploads/2022/04/22141927/Small-Business-Job-Creation-Fact-Sheet-Apr2022.pdf>.
- 26 See U.S. Small Business Administration Office of Advocacy, “2022 Small Business Profile,” (2022) at 1, available at <https://cdn.advocacy.sba.gov/wp-content/uploads/2022/08/30121338/Small-Business-Economic-Profile-US.pdf>.
- 27 See Jeffrey M. Jones, “Confidence in U.S. Institutions Down; Average at New Low,” (July 5, 2022) available at <https://news.gallup.com/poll/394283/confidence-institutions-down-average-new-low.aspx> (noting that 68% of Americans have confidence in small businesses). Major US Institutions included in survey: Small business, military, police, medical system, church or organized religion, public schools, organized labor, banks, large technology companies, U.S. Supreme Court, presidency, newspapers, criminal justice system, Big business, Television news, and Congress. See Gallup, “Confidence in Institutions,” (2022) available at <https://news.gallup.com/poll/1597/confidence-institutions.aspx>.
- 28 See Ewing Marion Kauffman Foundation, “America’s New Business Plan,” (2022) at 12, available at [https://www.startupnow.org/wp-content/uploads/sites/12/2022/05/ANBP-Refresh-Final\\_v3.pdf#page=12&zoom=100,0,0](https://www.startupnow.org/wp-content/uploads/sites/12/2022/05/ANBP-Refresh-Final_v3.pdf#page=12&zoom=100,0,0).
- 29 See Nasdaq Entrepreneurial Center, “Pay Ownership Valuation (POV) Research Findings,” (2022) at 7, available at [https://evidence2impact.psu.edu/wp-content/uploads/2022/07/POV-Final\\_Research.pdf](https://evidence2impact.psu.edu/wp-content/uploads/2022/07/POV-Final_Research.pdf).

- 30 See Small Business Majority, "Survey: Small Businesses Optimistic About the Future, Despite Concerns about Inflation and Barriers to Capital," (Oct. 13, 2022) at 2, available at <https://smallbusinessmajority.org/sites/default/files/research-reports/2022-SSIB-SBM-Network-Poll-Report.pdf>.
- 31 See Hello Alice, "Capital Access Temp Check," (Apr. 2022) at 1, available at <https://helloalice.com/wp-content/uploads/2022/05/APRIL-Capital-Access-Temp-Check.pdf>.
- 32 *Id.*
- 33 *Id.* at 3.
- 34 See January Ventures, "2021 Early Stage Founder Sentiment Report," (2021) at 9, available at [https://34a0404e-3457-4b9f-8fcc-19732fc72efe.filesusr.com/ugd/8d7061\\_f955eda79ba40bba50fcca2a2ebbd53.pdf](https://34a0404e-3457-4b9f-8fcc-19732fc72efe.filesusr.com/ugd/8d7061_f955eda79ba40bba50fcca2a2ebbd53.pdf).
- 35 See Ewing Marion Kauffman Foundation, *supra* note 28, at 20.
- 36 *Id.*
- 37 See The White House, "The Small Business Boom Under the Biden-Harris Administration," (Apr. 2022) at 1, available at [https://www.cdfa.net/r/WhiteHouse\\_04-2022\\_Business-Boom-Under-Biden-Harris-Administration.html](https://www.cdfa.net/r/WhiteHouse_04-2022_Business-Boom-Under-Biden-Harris-Administration.html).
- 38 See Economic Innovation Group, "More Physical Places of Businesses Open Now than Pre-Pandemic, Led by Sun Belt Metros," (Apr. 5, 2022) available at <https://indicators.kauffman.org/wp-content/uploads/sites/2/2022/03/2021-Early-State-Entrepreneurship-National-Report.pdf>. By contrast, only 44 percent of counties had reached a similar milestone five full years after the onset of the Great Recession.
- 39 See Robert Fairlie, "National Report on Early-Stage Entrepreneurship in the United States: 2021," (Mar. 2022) at 19, available at <https://indicators.kauffman.org/wp-content/uploads/sites/2/2022/03/2021-Early-State-Entrepreneurship-National-Report.pdf>.
- 40 See Federal Reserve Banks, "Small Business Credit Survey. 2022 Report on Employer Firms," (Feb. 22, 2022) at 7, available at <https://www.fedsmallbusiness.org/survey/2022/report-on-employer-firms>.
- 41 *Id.* at i.
- 42 *Id.* at 7. In addition, 45% cut staff hours or downsized operations, 28% altered their payments or did not make a payment, and 2% reported no action in response to the challenges.
- 43 *Id.* at 19. Percentages add to more than 100 because respondents could select multiple options. Unlike prior years, the Federal Reserve's Small Business Credit survey did not include data about the use of retained earnings for ongoing business operations.
- 44 *Id.* at ii, 14-17. In 2021, 42% of businesses made their need met, a decline from 47% of businesses in 2020.
- 45 *Id.* at ii, 16-17.
- 46 See Jeffrey Sohl, "The Angel Market in 2021: Metrics Indicate Strong Market," *Center for Venture Research*, (May 20, 2022) at 1, available at [https://paulcollege.unh.edu/sites/default/files/resource/files/fy\\_2021\\_analysis\\_report\\_final.pdf](https://paulcollege.unh.edu/sites/default/files/resource/files/fy_2021_analysis_report_final.pdf).
- 47 *Id.* at 1.
- 48 *Id.*
- 49 *Id.* at 2.
- 50 See Angel Capital Association, "Angel Funders Report 2022," (Nov. 2022) at 10, available at <https://www.angelcapitalassociation.org/angel-funders-report-2022/>.
- 51 *Id.* at 14.
- 52 See Jeffrey Sohl, *supra* note 46, at 1.
- 53 *Id.* at 2.
- 54 See Angel Capital Association, *supra* note 50, at 36.
- 55 *Id.* at 12.
- 56 See "Seed Round" available at <https://www.sec.gov/jargon-z#S>.
- 57 See PitchBook-NVCA, "Venture Monitor Q2 2022," (July 13, 2022) at 8, available at <https://pitchbook.com/news/reports/q2-2022-pitchbook-nvca-venture-monitor>.
- 58 See Samir Kaji, "Why Emerging Managers have Become a Staple of LP Portfolios," *Venture Unlocked* (Aug. 11, 2022) available at <https://ventureunlocked.substack.com/p/why-emerging-managers-are-a-critical>; see also Gené Teare, "How Seed Funding Has Exploded in the Past 10 Years," (Oct. 28, 2021) available at <https://news.crunchbase.com/venture/seed-funding-startups-top-vc-firms-a16z-nea-khosla/>.
- 59 See Samir Kaji, *supra* note 58 (providing 2022 estimate); see CBInsights, "The 106 Most Active Seed Venture Capital Firms," (Jan. 10, 2015) available at <https://www.cbinsights.com/research/active-seed-venture-capital-firms-2014/> (providing number of active U.S. seed VC investors as of 2010-2014).
- 60 See PitchBook-NVCA, *supra* note 57, at 8. Excel "Angel & Seed Activity" tab.

- 61 See Dropbox DocuSend, “The Pre-Seed Round in 2021-22. Adapting the Pitch Deck for a New Market,” (Aug. 17, 2022) at 10, available at <https://try.docsend.com/fundraising-report>; see Dropbox DocuSend, “The Seed Round in 2021-22. Proving Market Fit and Monetization Amid Uncertainty,” (Nov. 2022) at 11, available at <https://try.docsend.com/seed-fundraising-report>.
- 62 See Dropbox DocuSend, “The Pre-Seed Round in 2021-22. Adapting the Pitch Deck for a New Market,” *supra* note 61, at 10.
- 63 See Dropbox DocuSend, “The Pre-Seed Round in 2021-22. Adapting the Pitch Deck for a New Market,” *supra* note 61, at 21; see Dropbox DocuSend, “The Seed Round in 2021-22. Proving Market Fit and Monetization Amid Uncertainty,” *supra* note 61, at 22.
- 64 See Dropbox DocuSend, “The Pre-Seed Round in 2021-22. Adapting the Pitch Deck for a New Market,” *supra* note 61, at 18.
- 65 *Id.* at 3-4.
- 66 See Dropbox DocuSend, “The Seed Round in 2020-21. Make or Break Moment for Founders,” (2021) at 19, available at <https://try.docsend.com/seed-fundraising-report>.
- 67 See Jeffrey Sohl, *supra* note 46, at 2.
- 68 See PitchBook-NVCA, *supra* note 57. Excel “Angel & Seed Activity” tab. This graph depicts the combined the Angel and Seed market. However, the angel market constitutes a small part of the combined market values. From 2018 to Jun. 30, 2022, the angel activity was between 13% and 5% of the combined angel and seed market value reflected in the graph.
- 69 *Id.* at 8.
- 70 *Id.*
- 71 See PitchBook-NVCA, “Venture Monitor Q1 2022 (Apr. 13, 2022) at 9, available at <https://pitchbook.com/news/reports/q1-2022-pitchbook-nvca-venture-monitor>. Excel “Fundraising Activity” tab; see Kyle Stanford, “Micro-Funding Opportunity. Micro-Funds Proliferate in a Market Where Everything is Getting Larger,” *PitchBook* (Apr. 5, 2022) at 2-3, available at [https://files.pitchbook.com/website/files/pdf/Q2\\_2022\\_PitchBook\\_Analyst\\_Note\\_Micro-Funding\\_Opportunity.pdf](https://files.pitchbook.com/website/files/pdf/Q2_2022_PitchBook_Analyst_Note_Micro-Funding_Opportunity.pdf).
- 72 See Kyle Stanford, *supra* note 71, at 8.
- 73 *Id.* at 6.
- 74 See Angel Resource Institute, “HALO Report. Annual Report on Angel Investments (2021) at 4, available at <https://angelresourceinstitute.org/reports/HALO2021.pdf>; see Kyle Stanford, *supra* note 71, at 5.
- 75 Regions that do not have data available are shown in white with an outline. See Angel Resource Institute, *supra* note 74, at 7. The overall percent of in-region investments was 75% in 2020 and 60% in 2019. See Angel Resource Institute, “HALO Report. Annual Report on Angel Investments,” (2020) at 6, available at <https://angelresourceinstitute.org/reports/HALO2020.pdf>.
- 76 See Kyle Stanford, *supra* note 71, at 5.
- 77 *Id.*
- 78 See Kenan Institute of Private Enterprise, “Capital Ecosystems: Seeding Small and Regional Funds to Increase Opportunity,” (June 1, 2022) available at <https://kenaninstitute.unc.edu/kenan-insight/capital-ecosystems-seeding-smaller-and-regional-funds-to-increase-opportunity/>.
- 79 See PitchBook-NVCA, *supra* note 57. Excel “Deals x State” tab.
- 80 *Id.* The top three states for VC funding are California, New York, and Massachusetts.
- 81 See Venture Forward, “Employment Dynamics at VC-Backed Companies in the United States: 1990 to 2020,” (Feb. 15, 2022) available at <https://ventureforward.org/resources/employment-dynamics/>.
- 82 See NVCA, *supra* note 24, at 10; see also Venture Forward, “Venture 101,” (2022) available at <https://ventureforward.org/education/venture-101/>.
- 83 See NVCA, *supra* note 24, at 10.
- 84 *Id.*
- 85 See Natee Amornsiripanitch *et al.*, “More than Money: Venture Capitalists on Boards,” *The Journal of Law, Economics, and Organization* (Apr. 11, 2019) at 5, available at [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2586592](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2586592).
- 86 See Jeremy Greenwood *et al.*, “Venture Capital: A Catalyst for Innovation and Growth,” (Apr. 21, 2022) at 3, available at <https://files.stlouisfed.org/files/htdocs/publications/review/2022/04/06/venture-capital-a-catalyst-for-innovation-and-growth.pdf>.
- 87 See PitchBook-NVCA, *supra* note 57, at 31.
- 88 See Marina Tempkin, “VCs Hit with ‘Fundraising Pain’ as LPs Deal with Venture Overexposure,” *PitchBook* (May 5, 2022) available at <https://pitchbook.com/news/articles/vc-fundraising-venture-capital-asset-allocation-lp-gp-diligence>.

- 89 See Will Gornall and Ilya A. Strebulae, “The Economic Impact of Venture Capital: Evidence from Public Companies,” (June 2021) at 7, available at [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2681841](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2681841) (noting that census data show 4.3 million business formations in 2020 (31 million over the past decade), while PitchBook data show 3,842 companies received their first VC financing in 2020 (35 thousand over the past decade)).
- 90 See NVCA, *supra* note 24, at 8. Data from PitchBook-NVCA, *supra* note 57. Excel “Median Deal Size” tab. Average exit value is calculated from the exit value and exit count. See Venture Forward, *supra* note 81.
- 91 See PitchBook-NVCA, *supra* note 57, at 3.
- 92 *Id.* Excel “Deal Activity” tab.
- 93 *Id.* Excel “Angel and Seed Activity”, “Early Stage Activity” and “Late Stage Activity” tabs.
- 94 *Id.* at 14. Excel “Median Deal Size” tab; see also Lian Chang, “State of Private Markets,” *Carta* (Aug. 19, 2022) available at <https://carta.com/blog/state-of-private-markets-q2-2022/> (regarding the relative stagnation of post-money valuations at Series C, D and E+ levels).
- 95 See Lian Chang, *supra* note 94.
- 96 See PitchBook-NVCA, *supra* note 57. Excel “Fundraising x Size” tab; see Priyamvada Mathur, “US Venture Capital Trends in Five Charts,” *PitchBook*, (July 15, 2022) available at <https://pitchbook.com/news/articles/venture-monitor-vc-trends-charts>.
- 97 See PitchBook-NVCA, “Q1 2022 PitchBook NVCA Venture Monitor First Look. VC Industry Facing Market Full of Headwinds,” (Apr. 5, 2022) at 2, available at [https://files.pitchbook.com/website/files/pdf/Q1\\_2022\\_PitchBook\\_NVCA\\_Venture\\_Monitor\\_First\\_Look.pdf](https://files.pitchbook.com/website/files/pdf/Q1_2022_PitchBook_NVCA_Venture_Monitor_First_Look.pdf).
- 98 See PitchBook-NVCA, *supra* note 57, at 35. Excel “Emerging vs. Experienced Funds” tab. Emerging is defined as firms that have launched fewer than four funds and Experienced firms are defined as firms that have opened four or more funds.
- 99 *Id.*
- 100 See Silicon Valley Bank, “Global Fund Banking Outlook Report,” (Q3 2022) at 12, available at <https://www.svb.com/globalassets/trendsandinsights/reports/global-fund-banking-outlook/q3-2022/gfb-report-q3-2022-9722.pdf>.
- 101 *Id.* Respondents to the survey can choose up to three options.
- 102 *Id.*
- 103 *Id.* Respondents to the survey can choose up to three options.
- 104 *Id.*
- 105 *Id.* See also Michael Maziar, “Rising Tech Hubs Mean New Opportunities for Emerging Managers,” *Silicon Valley Bank* (Oct. 4, 2022) available at <https://www.svb.com/emerging-manager-insights/scaling-for-success/rising-tech-hubs-for-emerging-managers>; see also Waverly Deutsch, “Women and Minority Investors Are Taking Matters into Their Own Hands,” *Chicago Booth Review* (May 10, 2021) available at <https://www.chicagobooth.edu/review/women-and-minority-investors-are-taking-matters-their-own-hands>.
- 106 See PitchBook-NVCA, *supra* note 57, at 19; see also James Thorne, “Corporate VC Firms Buck ‘Tourist’ Reputation with Pandemic Dealmaking,” *PitchBook*, (Sept. 28, 2020) available at <https://pitchbook.com/news/articles/corporate-vc-firms-pandemic-dealmaking-rate-bucks-tourist-reputation>; see also James Thorne, “What’s Driving Private Equity’s March on VC?,” *PitchBook*, (Sept. 8, 2021) available at <https://pitchbook.com/news/articles/private-equity-nontraditional-investors-vc-deals>; see also Cameron Stanfill *et al.*, “Crossing Over Into Venture,” *PitchBook*, (Apr. 20, 2021) at 2, available at <https://pitchbook.com/news/reports/q2-2021-pitchbook-analyst-note-crossing-over-into-venture>.
- 107 See PitchBook-NVCA, *supra* note 57. Excel “Alternative VC” tab.
- 108 *Id.* at 30. Excel “Alternative VC” tab; see Richard Waters, “Venture Capital’s Silent Crash: When the Tech Boom met Reality,” *Financial Times* (Aug. 1, 2022) available at <https://www.ft.com/content/6395df7e-1bab-4ea1-a7ea-afaa71354fa0>.
- 109 See PitchBook, “US VC Valuations Report,” (Feb. 4, 2022) at 17, available at [https://files.pitchbook.com/website/files/pdf/2021\\_Annual\\_US\\_VC\\_Valuations\\_Report.pdf](https://files.pitchbook.com/website/files/pdf/2021_Annual_US_VC_Valuations_Report.pdf).
- 110 See Miriam Gottfried and Laura Cooper, “Buyout Firms Seek \$1 Trillion of New Funding Even as Markets Drop and Deal-Making Dries Up,” *The Wall Street Journal* (July 18, 2022) available at <https://www.wsj.com/articles/buyout-firms-seek-1-trillion-of-new-funding-even-as-markets-drop-and-deal-making-dries-up-11658136602>.

- 111 See Marina Tempkin, *supra* note 88.
- 112 See PitchBook-NVCA, *supra* note 57, at 31. Excel “Exits x Type” tab.
- 113 *Id.* at 32. Excel “Exits x Previous Round” tab.
- 114 Includes issuers with a market capitalization of \$250 million or less.
- 115 Data on U.S. listed domestic firms was estimated by DERA based on the Center for Research in Security Prices (CRSP) database. The analysis includes U.S. common stocks (share codes 10 and 11) listed on NYSE, NYSE MKT and Nasdaq. The analysis excludes investment funds and trusts (Standard Industrial Classification codes 6722, 6726, 6798, and 6799). A company with several classes of shares is counted once. Data for 2022 represents the number of listed firms and market capitalization as of June 30, 2022.
- 116 See *supra* note 115 for a description of the methodology used to calculate this data.
- 117 This graphic is based on DERA data, including pooled funds. This data was collected from Thomson Financial’s SDC Platinum database. IPOs by small companies include IPOs by U.S. companies that after the non-SPAC offering have a size less than or equal to \$250 million, calculated by multiplying price of the company’s stock at the close of the day of the offering by the number of outstanding shares on the day of the offering. IPOs by large companies include IPOs by companies that after the non-SPAC offering have a size greater than \$250 million, calculated as described above. Data from the Center for Research in Securities Prices (CRSP), Dealogic, and Compustat were used to fill in missing information from SDC Platinum. Those companies with missing either (1) a stock price on the day of the offering or (2) a number of outstanding shares are not included in the statistics. The estimates provided in this graph for small public companies are based on the estimated market capitalization for the issuer on the date of the offering as provided in the above-listed databases. There have been significant downward revisions in the most recent estimates as the market capitalization of issuers are corrected in the databases.
- 118 See *supra* note 117 for a description of the methodology used to calculate this data. The number shown on the top of the bar represents the total number of IPOs. The percentages not illustrated are IPOs by small foreign companies. See also Tom Zanki, “Small IPOs Buck Trends in an Otherwise Cold Market,” *Law 360*, (Aug. 24, 2022) available at <https://www.law360.com/banking/articles/1523843/small-ipos-buck-trends-in-an-otherwise-cold-market>.
- 119 See Will Gornall and Ilya A. Strebulae, *supra* note 89, at 17. The study used market capitalization and enterprise value as of December 31, 2020. All other variables, including research and development dollar amount and number of patents, are from Compustat as of 2020 or the most recent fiscal year. VC classifications are from PitchBook, Thomson ONE, VentureSource, and manual matching.
- 120 See Jeremy Greenwood *et al.*, *supra* note 86, at 7. This study is based on U.S. public companies between 1970 and 2014.
- 121 See “Smaller Reporting Company Definition,” Release Nos. 33-10513; 34-83550; File No. S7-12-16 (June 28, 2018) available at <https://www.sec.gov/rules/final/2018/33-10513.pdf>.
- 122 See “Pay Ratio Disclosure,” Release Nos. 33-9452; 34-70443; File No. S7-07-13 (Aug. 5, 2015) at 89, available at <https://www.sec.gov/rules/proposed/2013/33-9452.pdf> (providing estimates of the number of annual reports on Form 10-K based on a review of EDGAR filings in 2011). For comparability with the 2011 data, DERA staff estimated the number of annual reports on Form 10-K filed in 2021 based on a review of EDGAR filings.
- 123 See Bill Hertz, “The Microcap Universe: Overview and Opportunities,” Nasdaq, (June 7, 2022) available at <https://www.nasdaq.com/articles/the-micro-cap-universe%3A-overview-and-opportunities>; see also, Todd Lincoln, MBA, “What is Market Cap? Everything You Need to Know,” *Medium*, (Jan. 15, 2021) available at <https://medium.com/the-investors-handbook/market-cap-a474214c1368> (defining micro-cap as companies with market cap between \$0M and \$300 million, and small-cap as companies with market cap between \$300M and \$2 billion).

- 124 This graphic is based on DERA data. Registered offering data includes IPOs and registered secondary equity offerings, and was collected from Thomson Financial's SDC Platinum database. Registered debt offerings have been excluded. Small public companies include U.S. public companies with a size less than or equal to \$250 million on the date of the offering, calculated by multiplying the price of the company's stock at the close of the day of the offering by the number of outstanding shares on the day of the offering. Data from CRSP, Dealogic, and Compustat were used to fill in missing information from SDC Platinum. Those companies with missing either (1) a stock price on the day of the offering or (2) a number of outstanding shares are not included in the statistics. The estimates provided in this graph for small public companies are based on the estimated market capitalization for the issuer on the date of the offering as provided in the above-listed databases. There have been significant downward revisions in the most recent estimates as the market capitalization of issuers are corrected in the databases.
- 125 See *supra* note 124 for a description of the methodology used to estimate registered equity offerings by small public companies. This graphic includes the top industries based on the total proceeds raised in registered equity offerings by small public company during one of the respective periods, excluding offerings filed by pooled funds. Offerings for industries outside of these top industries accounted for approximately \$0.9 billion and \$0.3 billion in the twelve months ended June 2021 and 2022, respectively. Offerings by pooled funds, including SPACs, accounted for approximately \$17 billion and \$17 billion in the twelve months ended 2021 and 2022, respectively.
- 126 See "Accelerated Filer and Large Accelerated Filer Definitions," Release No. 34-88365; File No. S7-06-19," (Apr. 23, 2020) at 39, available at <https://www.sec.gov/rules/final/2020/34-88365.pdf> (amending the accelerated and large accelerated definitions).
- 127 See Protiviti Global Business Consulting, "SOX Compliance Amid Rising Costs, Labor Shortages and Other Post-Pandemic Challenges (June 9, 2022) at 5, available at [https://www.protiviti.com/sites/default/files/2022-10/protiviti\\_2022-sox-compliance-survey\\_global.pdf](https://www.protiviti.com/sites/default/files/2022-10/protiviti_2022-sox-compliance-survey_global.pdf).
- 128 *Id.* Excludes external audit-related fees.
- 129 See U.S. Securities and Exchange Commission, "Staff Report on the Issues Affecting the Provision of and Reliance Upon Investment Research Into Small Issuers," (Feb. 18, 2022) at 7, available at <https://www.sec.gov/files/staff-report-investment-research-small-issuers.pdf>; see also Todd Lincoln, MBA, *supra* note 123.
- 130 See U.S. Securities and Exchange Commission, *supra* note 129, at 7. The Congressional Research Report defines small issuers as companies with market capitalization ranging up to \$250 million, and large issuers as companies with market capitalization above \$250 million.
- 131 *Id.* at 11-12, 45-46.
- 132 See IR Magazine, "Sample: Retail Investors Research Report Sponsored by Broadridge," (Aug. 2021) at 3, 5, available at [https://www.thecorporatecounsel.net/member/memos/Broadridge/08\\_21\\_report.pdf](https://www.thecorporatecounsel.net/member/memos/Broadridge/08_21_report.pdf). See Garnet Roach, "Only Small Caps See Minority of Shares Held by Institutions, Research Shows," *IR Magazine*, (Jan. 18, 2022) available at <https://www.irmagazine.com/small-cap/only-small-caps-see-minority-shares-held-institutions-shows-research>.
- 133 See U.S. Small Business Administration Office of Advocacy, *supra* note 26, at 3. Ownership includes equal and majority ownership.
- 134 *Id.* Ownership includes equal and majority ownership.
- 135 See PitchBook, "All In. Female Founders in the US VC Ecosystem," (Nov. 2, 2022) at 4, available at <https://pitchbook.com/news/reports/2022-all-in-female-founders-in-the-us-vc-ecosystem>. Women-founded includes companies with at least one woman founder. Deal count is in Excel "VC deal activity" tab.
- 136 See Carta, "Annual Equity Report 2021," (Dec. 8, 2021) at 13, available at <https://carta.com/equity-summit/reports/2021/>.
- 137 See [https://data.census.gov/table?q=ab1900\\*&ctid=ABSCB2019.AB1900CSCB01&hidePreview=true&nk=Q-DESC-B01](https://data.census.gov/table?q=ab1900*&ctid=ABSCB2019.AB1900CSCB01&hidePreview=true&nk=Q-DESC-B01). Percentages may not add to 100% due to rounding. Ownership includes majority ownership.
- 138 See Robert Fairlie, *supra* note 39, at 8. See also Ewing Marion Kauffman Foundation, "Who is the Entrepreneur? New Entrepreneurs in the United States, 1996-2021," (2022) at 1, available at [https://www.kauffman.org/wp-content/uploads/2022/10/Kauffman\\_Trends-in-Entrepreneurship-Who-Is-The-Entrepreneur-2021.pdf](https://www.kauffman.org/wp-content/uploads/2022/10/Kauffman_Trends-in-Entrepreneurship-Who-Is-The-Entrepreneur-2021.pdf) (noting that 39.9% of new entrepreneurs in 2021 were women).

- 139 See January Ventures, *supra* note 34, at 7.  
 140 *Id.* at 10.  
 141 See Kate Davidson and Aubree Eliza Weaver, “We Have a Lot of Work to do: Women and the Economy,” *Politico Morning Money* (June 29, 2022) available at <https://www.politico.com/newsletters/morning-money/2022/06/29/we-have-a-lot-of-work-to-do-women-and-the-economy-00043029>.  
 142 See Jeffrey Sohl, *supra* note 46, at 2.  
 143 *Id.*  
 144 See PitchBook-NVCA, *supra* note 57. Excel “Female Founder Activity” tab.  
 145 *Id.*  
 146 *Id.* Excel “Female Founder Activity” tab and “Deal Activity” tab.  
 147 *Id.* Excel “Female Founder Activity” tab.  
 148 See Carta, *supra* note 136, at 14.  
 149 See Jordan Rubio, “Check Out Where Female Founder Fundraising is Growing Fastest in the US,” *PitchBook* (Sept. 6, 2022) available at <https://pitchbook.com/news/articles/female-founders-metro-growth>. The percentage illustrates the growth in capital raised from 2020 to present compared to 2008-2019.  
 150 See Dropbox DocSend, “The Funding Divide 2022. Underrepresented Founders Get More Attention, but for Most, the Dollars Don’t Deliver,” (2022) at 3, available at <https://try.docsend.com/funding-divide-report>.  
 151 *Id.* at 6. See Justin Izzo, “Gains in Fundraising Can’t Shake Off the Losses for Female and Minority Founders in 2021,” *Dropbox DocSend* (Mar. 29, 2022) available at <https://www.docsend.com/blog/fundraising-gains-still-result-in-losses-for-female-and-minority-founders/>.  
 152 See Dropbox DocSend, *supra* note 150, at 9-10.  
 153 *Id.* at 10.  
 154 See Engine, “Making the Startup Ecosystem More Equitable,” (Nov. 2021) at “Introduction”, available at <https://static1.squarespace.com/static/571681753c44d835a440c8b5/t/6193d03ac7eb9c40442a6740/1637077051416/Making+the+Startup+Ecosystem+More+Equitable+11.15.pdf>.  
 155 See All Raise, “Against the Odds: Underrepresented Founders Report Positive Outlook on Business Despite Extra COVID-19 Pressures,” available at [https://www.allraise.org/assets/gms069\\_infographic\\_desktop\\_1400px.jpg](https://www.allraise.org/assets/gms069_infographic_desktop_1400px.jpg). See also Juliana Garaizer, “The Rising Tide: A “Learning-By-Investing” Initiative to Bridge the Gender Gap,” *Kauffman Fellows Report*, (2016) at 53-54, available at [http://www.kauffmanfellows.org/wp-content/uploads/KFR\\_Vol7/Juliana\\_Garaizer\\_vol7.pdf](http://www.kauffmanfellows.org/wp-content/uploads/KFR_Vol7/Juliana_Garaizer_vol7.pdf).  
 156 See Yahoo! Finance, “PitchBook Report on Women in VC Ecosystem Highlights Resilience and Strong Performance of Female Founders Amid Market Headwinds (Nov. 3, 2022) available at <https://finance.yahoo.com/news/pitchbook-report-women-vc-ecosystem-040100985.html?guccounter=1>; see PitchBook, *supra* note 135, at 21.  
 157 See Chengwei Liu *et al.* “The Case for Investing in Underdogs,” *Harvard Business Review* (July 18, 2022) available at <https://hbr.org/2022/07/the-case-for-investing-in-underdogs>.  
 158 See Carta, *supra* note 136, at 10.  
 159 See Ann Shepherd, “2021 Study of Gender Diversity on Private Company Boards,” *Crunchbase News*, (Mar. 29, 2022) available at <https://news.crunchbase.com/business/hum-for-her-2021-diversity-study-private-company-boards/>; see Ann Shepherd and Gené Teare, “2020 Study of Gender Diversity on Private Company Boards,” *Crunchbase News* (Mar. 1, 2021) available at <https://news.crunchbase.com/diversity/2020-diversity-study-on-private-company-boards/>.  
 160 See Priyamvada Mathur, “Charting Female Founders’ Standout Year for VC Exits,” *PitchBook* (Feb. 18, 2022) available at <https://pitchbook.com/news/articles/female-founders-venture-capital-exits-charts>. See PitchBook-NVCA, *supra* note 57. Excel “Exit x Type” tab.  
 161 See “50/50 Women on Boards, “2022 Gender Diversity Index Report,” (Sept. 9, 2022) at 3-4, 7, 9, available at [https://5050wob.com/wp-content/uploads/2022/09/5050WOB\\_Q2\\_2022\\_GDI\\_Annual\\_Report.pdf](https://5050wob.com/wp-content/uploads/2022/09/5050WOB_Q2_2022_GDI_Annual_Report.pdf). See also Alexandra Olson and the Associated Press, “Women Hold a Record Number of Corporate Board Seats. The Bad News: It’s Barely over 25%, and It’s Slowing Down,” *Fortune* (Sept. 30, 2022) available at <https://fortune.com/2022/09/30/how-many-women-sit-corporate-boards-record-28-percent-russell-3000/>. Data is as of June 30, 2022.  
 162 See Ryan Hibbison, “Female Founders Prove Resilient as They Seek Equal Share of VC Dollars,” *Venture Capital Journal* (Nov. 3, 2022) available at <https://www.venturecapitaljournal.com/female-founders-prove-resilient-as-they-seek-equal-share-of-vc-dollars/>.  
 163 See Jeffrey Sohl, *supra* note 46, at 2.  
 164 *Id.*  
 165 See Gené Teare, “Something Ventured: Female-Founded U.S. Venture Firms on Track to Raise over \$7B in 2021,” *Crunchbase News* (Nov. 10, 2021) available at <https://news.crunchbase.com/venture/female-founded-vc-firms-funds-data-2021-something-ventured/>.

- 166 See All Raise, “All Raise x Crunchbase VC Checkwriter Dashboard”, (as of 6/15/2022) available at <https://allraise.org/all-raise-x-crunchbase-vc-checkwriter-dashboard>. Per the All Raise x Crunchbase VC Checkwriter Dashboard, checkwriters are defined as those who can write checks, lead deals, and sit on boards. They are identified by their senior role within their firm (founder/co-founder, general partner, managing director or managing partner) and/or by a combination of the partner title and function as identified through board seats, press releases or deal association. This Dashboard tracks U.S.-based venture capital firms with over \$25 million dollars in AUM.
- 167 See Imani Augustus, “Women Wanted: The Equity Gap in Venture Capital,” *Alliance for Entrepreneurial Equity* (Mar. 22, 2022) available at <https://www.aeequity.org/product/women-wanted-the-equity-gap-in-venture-capital>. This article was published by Third Way available at ([www.thirdway.org](http://www.thirdway.org)).
- 168 See Yahoo! Finance, *supra* note 156; see also PitchBook, *supra* note 135, at 25.
- 169 See Imani Augustus, *supra* note 167.
- 170 See Aditya Aladangady and Akila Forde, “Wealth Inequality and the Racial Wealth Gap,” *Board of Governors of the Federal Reserve*, (Oct. 22, 2021) at Figure 1, available at <https://www.federalreserve.gov/econres/notes/feds-notes/wealth-inequality-and-the-racial-wealth-gap-20211022.html#fig1>. In this data set, primary residence is included in a household’s net worth (see Figure 3). “White,” “Black/African American” and “Other” excludes any respondents indicating Hispanic/Latino. “Other” includes Asian American/Pacific Islander, Native American/Alaska Native, Native Hawaiian, other race, and all respondents reporting more than one racial identification. Because of small sample sizes, there was not statistical power to further disaggregate this group of families. In 2019, families reporting more than one racial identification were the largest subgroup of the other or multiple race group (about 69 percent of families), followed by Asian families (about 23 percent of families). Because of the varied composition of the other group and changes in its composition over time, readers should exercise caution when making inferences. See Neil Bhutta *et al.*, “Disparities in Wealth by Race and Ethnicity in the 2019 Survey of Consumer Finances,” *Board of Governors of the Federal Reserve System*, (Sept. 28, 2020) at Figure 3, available at <https://www.federalreserve.gov/econres/notes/feds-notes/disparities-in-wealth-by-race-and-ethnicity-in-the-2019-survey-of-consumer-finances-20200928.html>.
- 171 *Id.*
- 172 See Kristen E. Broady, Ph.D and Cynthia Hester, Ph.D, “Reducing the Racial Financial Health Gap: The Opportunity for Responsible Fintech,” *PayPal*, (Sept. 30, 2021) at 8, available at <https://publicpolicy.paypal-corp.com/sites/default/files/2021-11/PP-Reducing-the-Racial-Financial-Health-Gap.pdf>.

- 173 See Federal Reserve Banks, "Economic Well-Being of U.S. Households in 2021," (May 2022) at 43-44, available at <https://www.federalreserve.gov/publications/files/2021-report-economic-well-being-us-households-202205.pdf>. "Fully banked" households had a bank account and, in the past 12 months, did not use any of the alternative financial services asked about in the survey. "Underbanked" households are those for whom the banking services they accessed appear to have been insufficient to meet their financial service needs. "Unbanked" households had no bank account; Less than 50% of unbanked households used alternative financial services.
- 174 See Kristen E. Broady, Ph.D and Cynthia Hester, Ph.D, *supra* note 172, at 12. See also Federal Reserve Banks, *supra* note 173, at 43.
- 175 See Chris Horymski, "What Is the Average Credit Score in the U.S.?", *Experian* (Feb. 22, 2022) available at <https://www.experian.com/blogs/ask-experian/what-is-the-average-credit-score-in-the-u-s/>.
- 176 See Kristen E. Broady, Ph.D and Cynthia Hester, Ph.D, *supra* note 172, at 12.
- 177 See Federal Reserve Banks, "Small Business Credit Survey: 2022 Report on Firms Owned by People of Color," (June 29, 2022) at 15, available at <https://www.fedsmbbusiness.org/survey/2022/2022-report-on-firms-owned-by-people-of-color>. Note: Findings for Native American-owned firms are omitted from this report because sample sizes are too small to make precise estimates for most measures.
- 178 See Quentin Brummet and Katie Johnson, "Understanding the American Entrepreneurial Landscape: A New Resource," *Entrepreneurship in the Population (EPOP)* (Oct. 19, 2022) at 6, available at [https://epop.norc.org/content/dam/epop/media/publications/pdf/epop2022-brief\\_american\\_entrepreneurship.pdf](https://epop.norc.org/content/dam/epop/media/publications/pdf/epop2022-brief_american_entrepreneurship.pdf). Note: "Other" includes non-Hispanic multi-race, non-Hispanic other reported races, and not reported.
- 179 See Babson College, "Global Entrepreneurship Monitor (GEM) 2021/2022 United States Report," (2022) at 70-73, available at <https://issuu.com/babsoncollege/docs/gem-2021-2022-us-report>.
- 180 *Id.* at 72-73. "Established business activity" is defined as ownership/management of businesses more than three and a half years old.
- 181 See Marc Morial and Jon Cowan, "America's Entrepreneurial Equity Crisis is Hurting the Economy," *Fortune*, (May 25, 2022) available at <https://fortune.com/2022/05/25/america-entrepreneurial-equity-crisis-hurting-economy-george-floyd-black-startups-business-discrimination-solutions-morial-cowan/>.
- 182 See Dropbox DocSend, *supra* note 150, at 10-11.
- 183 *Id.* at 11.
- 184 See Dropbox DocuSend, *supra* note 61, at 14-15.
- 185 See Jeffrey Sohl, *supra* note 46, at 2; see Jeffrey Sohl, "The Angel Market in 2020: Return of the Seed and Start-Up Stage Market for Angels," *Center for Venture Research*, (May 5, 2021) at 2, available at [https://paulcollege.unh.edu/sites/default/files/resource/files/2020-analysis-report\\_.pdf](https://paulcollege.unh.edu/sites/default/files/resource/files/2020-analysis-report_.pdf); see Jeffrey Sohl, "The Angel Market in 2019: Commitments by Angels Increase with a Significant Rise in Deal Valuations," *Center for Venture Research*, (May 5, 2020) at 2, available at <https://scholars.unh.edu/cgi/viewcontent.cgi?article=1032&context=cvr>.
- 186 See Jeffrey Sohl, *supra* note 46, at 2. See Jeffrey Sohl, *supra* note 185, at 2.
- 187 See Yoon Sun Hur, "Analysis of Capital Access for Entrepreneurs of Color," *Nasdaq Entrepreneurial Center Venture Equity Project*, (2022) available at <https://evidence2impact.psu.edu/project/pre-seed-and-seed-funding-for-entrepreneurs-of-color/>.
- 188 *Id.* See also Nasdaq Entrepreneurial Center, "The Venture Equity Project," (2022) available at <https://thecenter.nasdaq.org/vcp/>; see also Gené Teare, "Funding to Latine-Founded US Companies Falls Sharply in 2022," *Crunchbase News*, (Oct. 26, 2022) available at <https://news.crunchbase.com/diversity/us-based-latine-founded-companies-funding-falls/> (noting that Hispanic/Latino founders received 2.5% of VC dollars); see also Gené Teare, "VC Funding to Black-Founded Startups Slows Dramatically as Venture Investors Pull Back," *Crunchbase News*, (June 17, 2022) available at <https://news.crunchbase.com/diversity/vc-funding-black-founded-startups/> (noting that African American/Black founders received 1.3% of VC dollars).

- 189 See MetLife and U.S. Chamber of Commerce, "Special Report on Small Business and LGBTQ+ Inclusion," (June 9, 2022) at 5, available at [https://www.uschamber.com/assets/documents/SBI\\_PulseSurvey\\_June2022\\_Final\\_v4.pdf](https://www.uschamber.com/assets/documents/SBI_PulseSurvey_June2022_Final_v4.pdf).
- 190 See Hello Alice Report, "The LGBTQ+ Economy. A Closer Look at the Trends and Triumphs of New Majority Small Business Owners in 2022," (June 2022) at 11, available at [https://helloalice.com/wp-content/uploads/2022/06/LGBTQ-Economy-Report\\_Update.pdf](https://helloalice.com/wp-content/uploads/2022/06/LGBTQ-Economy-Report_Update.pdf).
- 191 See "LGBTQ-Owned Small Businesses in 2021. The Financial Health & Needs of LGBTQ Firms in the Small Business Credit Survey," *Center for LGBTQ Economic Advancement & Research and Movement Advancement Project*, (July 20, 2022) at 10, available at <https://lgbtq-economics.org/wp-content/uploads/2022/08/LGBTQ-Owned-Small-Businesses-in-2021-July-2022.pdf>. The report defined LGBTQ-owned businesses as those where individuals who identify as lesbian, gay, bisexual, transgender, or queer own 50% or more of the business.
- 192 See Diego Mariscal, "Entrepreneurship is a Pathway for Founders with Disabilities to Address Wealth and Employment Gaps", *Eveing Marion Kauffman Foundation*, (Oct. 26, 2022) available at <https://www.kauffman.org/currents/2gether-international-entrepreneurs-with-disabilities/>.
- 193 See National Disability Institute, "Small Business Ownership by People with Disabilities: Challenges and Opportunities," (Apr. 2022) at 12, available at <https://www.nationaldisabilityinstitute.org/wp-content/uploads/2022/07/ndi-small-business-research-report.pdf>.
- 194 *Id.*
- 195 *Id.* at 24. Roughly 24% did not apply for a loan due to a belief that they would be denied.
- 196 See Diego Mariscal, *supra* note 192.
- 197 See Jeffrey Sohl, *supra* note 46, at 1-2. See Jeffrey Sohl, *supra* note 185, at 2.
- 198 See Johan Cassel *et al.*, "Racial Diversity in Private Capital Fundraising," *National Bureau of Economic Research*, (Sept. 2022) at 2-3, available at [https://www.nber.org/system/files/working\\_papers/w30500/w30500.pdf](https://www.nber.org/system/files/working_papers/w30500/w30500.pdf) (citing <https://knightfoundation.org/reports/knight-diversity-of-asset-managers-research-series-industry/>).
- 199 See BLCK VC, "State of Black Venture. A Comprehensive Study of the Black Venture Ecosystem," (2022) at 13, available at <https://www.blckvc.org/state-black-venture>.
- 200 See Mahira Dayal, "The Most and Least Diverse Venture Capital Firms," *The Information's Diversity Index*, (Feb. 22, 2022) available at <https://www.theinformation.com/articles/the-most-and-least-diverse-venture-capital-firms>.
- 201 See BLCK VC, *supra* note 199, at 7.
- 202 See LATINX VC, "State of Latinx VCs. First Annual Report," at 3, available at [https://uploads-ssl.webflow.com/613a3a58a5fa7d03f5df48f6157581069a40d7e7375a2d\\_LatinxVCs\\_state.pdf](https://uploads-ssl.webflow.com/613a3a58a5fa7d03f5df48f6157581069a40d7e7375a2d_LatinxVCs_state.pdf).
- 203 See Mahira Dayal, *supra* note 200.
- 204 See LATINX VC, *supra* note 202, at 4.
- 205 See BLCK VC, *supra* note 199, at 18.
- 206 See Johan Cassel *et al.*, *supra* note 198, at 4, 6.
- 207 See BLCK VC, *supra* note 199, at 24.
- 208 See Diversity VC, "The Equity Record," (Nov. 9, 2022) at 16, available at <https://diversity.vc/diversity-vc-report-2022-usa/>.
- 209 Based on Russell 3000 company data. See ISS Insights, "Racial and Ethnic Diversity on U.S. Corporate Boards – Progress Since 2020 (July 26, 2022) available at <https://insights.issgovernance.com/posts/racial-and-ethnic-diversity-on-us-corporate-boards/>.
- 210 *Id.*
- 211 See Brianna Funderburk and Lucas Misera, "The Impact of Natural Disasters on Small Businesses," *Fed Small Business*, (Nov. 15, 2022) available at <https://www.fedsmallbusiness.org/analysis/2022/the-impact-of-natural-disasters-on-small-businesses>.
- 212 See Martin Hiti *et al.*, "Small Business Recovery After Natural Disasters," (Sept. 6, 2022) available at <https://libertystreeteconomics.newyorkfed.org/2022/09/small-business-recovery-after-natural-disasters/>.
- 213 See Martin Hiti *et al.*, "How do Natural Disasters Affect U.S. Small Business Owners," (Sept. 6, 2022) available at <https://libertystreeteconomics.newyorkfed.org/2022/09/how-do-natural-disasters-affect-u-s-small-business-owners/>.
- 214 See National Centers for Environmental Information, "Billion-Dollar Weather and Climate Disasters," (accessed December 6, 2022) available at [https://www.ncei.noaa.gov/access/billions/events/US/2022?disasters\[\]=all-disasters](https://www.ncei.noaa.gov/access/billions/events/US/2022?disasters[]=all-disasters). Note that NOAA tracks events on a calendar basis and we have combined natural disaster events that straddle calendar years.

- 215 The estimated losses cover the period from October 1, 2021 through September 30, 2022. See <https://www.ncei.noaa.gov/access/billions/events>. This estimate, however, does not include estimated losses from Hurricane Ian, which could cost insurers \$40 billion or more. See Chris Isidore, "Hurricane Ian could be Florida's Costliest Storm Ever," CNN, (Sept. 30, 2022) available at <https://www.cnn.com/2022/09/30/business/hurricane-ian-cost/index.html>. See Max Zahn, "Hurricane Ian Could Cause \$75 Billion in Damage," ABC News, (Oct. 3, 2022) available at <https://abcnews.go.com/Business/hurricane-ians-damage-reach-65-billion/story?id=90693223>.
- 216 See Federal Reserve Banks, *supra* note 40. Data from data appendix Excel tab "Disaster-impacted firms."
- 217 *Id.*
- 218 Data from the 2020 5-year American Community Survey (ACS) was used by DERA to estimate the population in zip codes affected by the natural disasters as described in *infra* note 219. However, certain zip codes were identified as missing population values, so the percentage is likely underestimated.
- 219 This graphic is based on DERA data. Evaluated from July 1, 2019 to June 30, 2022 using zip codes affected by natural disasters, excluding COVID-19 Pandemic. Zip codes designated as affected are defined as having one or more residents approved for housing assistance under FEMA's IHP program for natural disasters with classifications of Major Disaster Declaration and incident start dates between July 1, 2019 and June 30, 2022. Given the trailing impact caused by natural disasters, each zip code affected in that three year period was included. Classification of disaster areas are based on FEMA Disaster Declaration Summaries data and FEMA Housing Assistance Program Data available at <https://www.fema.gov/about/openfema/data-sets>, updated on September 15, 2022. The classification method for disaster areas is based on the methodology in the "2017 Small Business Credit Survey – Report on Disaster-Affected Firms," Federal Reserve Banks of Dallas, New York, Richmond, and San Francisco, available at <https://www.newyorkfed.org/medialibrary/media/smallbusiness/2017/SBCS-Report-on-Disaster-Affected-Firms.pdf>.
- 220 Evaluated from July 1, 2019 to June 30, 2022 using zip codes affected by natural disasters as described in *supra* note 219.
- 221 See Kenan Fikri, "Restoring Well-Being and Entrepreneurship in Rural America," *Federal Reserve Bank of St. Louis – Investing in Rural Prosperity*, (2021) at 99, available at <https://www.stlouisfed.org/community-development/publications/invest-in-rural>.
- 222 *Id.* at 97.
- 223 See U.S. Census, "2020 Business Dynamics Statistics Datasets" available at <https://www.census.gov/programs-surveys/bds.html>. Data pulled as of 11/15/2022. Specific data pulled: <https://www.census.gov/data/datasets/time-series/econ/bds/bds-datasets.html>. Metro/Non-Metro by Firm Age and Metro/Non-Metro.
- 224 See Deb Martin, "Fostering a Culture of Entrepreneurship and Innovation in Rural Communities," *Federal Reserve Bank of St. Louis – Investing in Rural Prosperity*, (2021) at 268, available at <https://www.stlouisfed.org/community-development/publications/invest-in-rural>.
- 225 See Federal Reserve Banks, *supra* note 40. Data from data appendix Excel "Geography" tab. The percentage of U.S. Rural Small Businesses is a percentage of the total U.S. rural small businesses broken down by Census division. The U.S. Rural Small Businesses will total 100%. The percentage of small businesses in the region is the percentage of small business that are rural as compared to all small businesses within each individual Census division. The small businesses in the region percentage was calculated based on the Fed Small Business Survey Employer Firms report data. Since the small businesses in the region percentage is based on a calculation within each Census region the aggregate percentages across the U.S. regions will not total 100%.
- 226 See Matt Dunne, "Small-Town Tech Towns: Where Scalable Entrepreneurship Is Propelling Rural Growth," *Federal Reserve Bank of St. Louis – Investing in Rural Prosperity*, (2021) at 320-322, available at <https://www.stlouisfed.org/community-development/publications/invest-in-rural>.
- 227 See Federal Reserve Banks, *supra* note 40. Data from data appendix Excel "Geography" tab.



- 248 Currently, for offerings of greater than \$124,000, but less than \$618,000, the issuer must provide financial statements that have been reviewed by a public accountant that is independent of the issuer.
- 249 See “Temporary Amendments to Regulation Crowdfunding,” Release No. 33-10781 (May 4, 2020), available at <https://www.sec.gov/rules/interim/2020/33-10781.pdf>.
- 250 See 17 CFR 227.100(b)(3) available at <https://www.ecfr.gov/current/title-17/chapter-II/part-227/subpart-A/section-227.100>.
- 251 See “Facilitating Capital Formation and Expanding Investment Opportunities by Improving Access to Capital in Private Markets,” Release Nos. 33-10884; 34-90300; IC-34082; File No. S7-05-20 (Nov. 2, 2020), available at <https://www.sec.gov/rules/final/2020/33-10884.pdf>.
- 252 See e.g., “State of Small Business Capital Formation” section of the Report above, at 13.
- 253 See, e.g., “Small and Emerging Businesses” section of the Report above, at 23.
- 254 See “Notice of Proposed Exemptive Order Granting Conditional Exemption from the Broker Registration Requirements of Section 15(a) of the Securities Exchange Act of 1934 for Certain Activities of Finders,” Release No. 34-90112; File No. S7-13-20, (Oct. 13, 2020) at 4, available at <https://www.sec.gov/rules/exorders/2020/34-90112.pdf>.
- 255 Market participants look at staff guidance when trying to determine whether broker registration is require. See Notice of Proposed Exemptive Order, *supra* note 254 at 15.
- 256 See, e.g., “Women Business Owners and Investors” section of the Report above, at 47-49; “Minority Business Owners and Investors” section of the Report above, at 57-58, and “Rural Communities” section of the Report above, at 66.
- 257 See *Ewing Marion Kauffman Foundation*, “Inclusive Entrepreneurial Ecosystems are our Moral and Economic Imperative,” (Oct. 19, 2022) available at <https://www.kauffman.org/currents/inclusive-entrepreneurial-ecosystems-moral-economic-imperative/>.
- 258 See Notice of Proposed Exemptive Order, *supra* note 254.
- 259 See U.S. Securities and Exchange Commission Agency Rule List (Spring 2022), *supra* note 243.
- 260 See “What Happens if a Startup Does not Comply with Securities Laws?” available at <https://www.sec.gov/education/capitalraising/building-blocks/noncompliance>.
- 261 See, e.g., “Small and Emerging Businesses” section of the Report above, at 23, and “Mature and Later-Stage Companies” section of the Report above, at 35.
- 262 See, e.g., “Small and Emerging Businesses” section of the Report above, at 29 and 30.
- 263 See, e.g., “Mature and Later-Stage Companies” section of the Report above, at 33.
- 264 See Transcript of the 41st Annual SEC Small Business Forum, *New Investor Voices: How Emerging Fund Managers Are Diversifying Capital* (April 6, 2022), available at <https://www.sec.gov/files/transcript-new-investor-voices.pdf>. See, e.g., “Small and Emerging Businesses” section of the Report above, at 29, and “Mature and Later-Stage Companies” section of the Report above, at 36.
- 265 See, e.g., “Mature and Later-Stage Companies” section of the Report above, at 36 and 38.
- 266 See, e.g., “Women Business Owners and Investors” section of the Report above, at 53, and “Minority Business Owners and Investors” section of the Report above, at 60.
- 267 See Transcript of the 41st Annual SEC Small Business Forum, *New Investor Voices*, *supra* note 264 at 27-29.
- 268 See Transcript of the 41st Annual SEC Small Business Forum, *New Investor Voices*, *supra* note 264 at 29.
- 269 See Letter from the SEC Small Business Capital Formation Advisory Committee to Chair Gary Gensler (May 20, 2021) available at <https://www.sec.gov/spotlight/sbcfac/encouraging-small-regional-funds-043021.pdf>.
- 270 See Transcript of the Small Business Capital Formation Advisory Committee Meeting, *Entrepreneurship Hubs and the IPO Market*, (Oct. 13, 2022) available at <https://www.sec.gov/info/smallbus/acsec/sbcfac-transcript-101322.pdf>.
- 271 See Transcript of the 41st Annual SEC Small Business Forum, *Small Cap World: What to Know and How to Think Ahead* (April 7, 2022) at 46, available at <https://www.sec.gov/files/transcript-small-cap-world.pdf>.

- 272 *See, e.g.*, “Rule 10b5-1 and Insider Trading,” Release Nos. 33-11013; 34-93782; File No. S7-20-21 (Jan. 13, 2022), *available at* <https://www.sec.gov/rules/proposed/2022/33-11013.pdf> (while the Commission did not propose to exempt smaller reporting companies from the new disclosures, those companies would be permitted to limit their disclosures consistent with the scaled approach to their executive compensation disclosures); “The Enhancement and Standardization of Climate-Related Disclosures for Investors,” Release Nos. 33-11042; 34-94478; File No. S7-10-22 (Mar. 21, 2022), *available at* <https://www.sec.gov/rules/proposed/2022/33-11042.pdf> (proposing to exempt smaller reporting companies from some of the new disclosure requirements, and proposing a delayed compliance date); “Pay Versus Performance,” Release No. 34-95607; File No. S7-07-15 (Aug. 25, 2022), *available at* <https://www.sec.gov/rules/final/2022/34-95607.pdf> (adopting scaled requirements for smaller reporting companies, but not delaying the compliance date for those companies).
- 273 *See, e.g.*, “Share Repurchase Disclosure Modernization,” Release No. 34-93783; IC-34440; File No. S7-21-21 (Dec. 15, 2021), *available at* <https://www.sec.gov/rules/proposed/2021/34-93783.pdf>; “Cybersecurity Risk Management, Strategy, Governance, and Incident Disclosure,” Release Nos. 33-11038; 34-94382; IC-34529; File No. S7-09-22 (Mar. 9, 2022), *available at* <https://www.sec.gov/rules/proposed/2022/33-11038.pdf>.
- 274 *See, e.g.*, “Small Public Companies” section of the Report above, at 43 and 44.
- 275 *See, e.g.*, “Small Public Companies” section of the Report above, at 39.
- 276 *See* Transcript of the Small Business Capital Formation Advisory Committee Meeting (May 6, 2022) at 53, *available at* <https://www.sec.gov/info/smallbus/acsec/sbcafe-transcript-050622.pdf>.





OFFICE OF THE  
ADVOCATE FOR SMALL  
BUSINESS CAPITAL  
FORMATION

U.S. Securities and  
Exchange Commission  
100 F Street NE  
Washington, DC 20549  
202.551.5407  
[www.sec.gov/oasb](http://www.sec.gov/oasb)  
[smallbusiness@sec.gov](mailto:smallbusiness@sec.gov)