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National Venture Capital Association

The Honorable Troy A. Paredes
Commissioner
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C.20549

Re: National Venture Capital Association

Dear Commissioner Paredes:

On behalf of the National Venture Capital Association, I would like to congratulate you on joining the Commission. It is my sincere hope that we will be able to work with you toward our mutual goals of investor protection and robust capital formation. NVCA consists of more than 450 venture capital firms which advocates for policies that are favorable to American innovation and entrepreneurship. It also provides objective research data to the public and works to maintain high professional standards for its members.

As I am sure you know, venture capital provides the start-up and development funding for many companies that go public on U.S. stock exchanges. In 2007 alone, venture capitalists invested approximately \$30 billion into small, high-risk, emerging growth companies in areas such as life sciences, information technology, homeland security, and clean technology. Until the recent "IPO drought" venture-backed companies have been a major portion of US IPOs on our national exchanges.

NVCA has played an active role in Commission policymaking over the past two decades. In addition to filing comment letters on various rulemakings, we have become personally involved in a number of ways. For example, Ted Schlein, the immediate past chairman of our board, was a member of the SEC's Advisory Committee on Smaller Public Companies. NVCA representatives have served on the Planning Committee of the Annual Small Business Capital Formation Forum for nearly a decade. NVCA also is engaged with not only the SEC, but the FASB, the PCAOB and the IASB on auditing and accounting issues.

In regard to regulatory policy, I would like to make you aware of the venture capital community's concerns with one of the outstanding rulemaking proposals at the Commission: the 2007 Regulation D proposal. You probably know that venture capital funds often raise money through the use of private offerings under SEC Regulation D. The Commission's 2007 proposal to modify Regulation D prompted NVCA to file the comment letter which I have attached. I believe our comment letter, which also incorporates a comment letter filed in an earlier related rulemaking, speaks for itself. I merely wish to call your attention to our comments on accredited investor standards, which are, for venture capital, the most important part of this multi-faceted rulemaking.

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I am enclosing a few of our most recent data publications for your reference. The enclosed information on the current state of the IPO market is of particular concern to NVCA. Should this situation persist, we would hope to meet with you and discuss it.

Again, please accept my best wishes for a rewarding tenure as a Commissioner and NVCA's sincere offer to be an open source of useful data and entrepreneurial perspective on the many policy choices facing the Commission.

Please do not hesitate to contact me or NVCA vice president, Jennifer Connell Dowling, (jcdowling@nvca.org, 703-524-2549) if we can be of assistance.

Sincerely yours,

A handwritten signature in black ink, appearing to read 'M. Heesen', with a long horizontal flourish extending to the right.

Mark G. Heesen
President



National Venture Capital Association

October 9, 2007

VIA E-Mail

Ms. Nancy M. Morris
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090
rule-comments@sec.gov

Re: *Release Nos. 33-8828; IC-27922, (File No. S7-18-07) Revisions of Limited Offering Exemptions in Regulation D.*

Background

The National Venture Capital Association (NVCA) represents the vast majority of American venture capital under management.¹ Venture capital funds provide start-up and development funding for innovative entrepreneurial businesses.

Venture capital plays a special role in fulfilling the purpose for which Regulation D was designed: facilitating capital formation. Indeed venture capital supports the ultimate goal of capital formation by promoting entrepreneurship, stimulating economic growth and creating jobs. These proven results of venture capital investments are a tangible manifestation of the somewhat abstract goal of “capital formation.”

¹ The National Venture Capital Association (NVCA) represents more than 480 venture capital firms. NVCA's mission is to foster greater understanding of the importance of venture capital to the US economy and support entrepreneurial activity and innovation. The NVCA represents the public policy interests of the venture capital community, strives to maintain high professional standards, provides reliable industry data, sponsors professional development, and facilitates interaction among its members. For more information about the NVCA, please visit www.nvca.org.

NVCA submitted a comment letter on March 7, 2007 on Release No. 33-8766; IA-2576; File No. S7-25-06, *Prohibition of Fraud by Advisers to Certain Pooled Investment Vehicles; Accredited Investors in Certain Private Investment Vehicles*, which is referred to as the Private Pooled Investment Vehicle Release in this Release. NVCA's March 7, 2007 comment letter² addresses some of the issues regarding qualifications for venture capital fund investors raised in the current Release on Regulation D (hereinafter "Regulation D Release"). Therefore, we incorporate those comments by reference into this letter.

Venture capital funds routinely raise investment capital through a private placement offered under the safe harbor Rule 506.³ Therefore, NVCA's members are very interested in modifications to Regulation D and support the Commission's efforts to provide additional flexibility for private offerings of securities. We strongly support the Commission's evaluation of its proposed rules in the Private Pooled Investment Vehicle Release (hereinafter "PPIV Release") that would create a separate accredited investor standard for private pooled investment vehicles within the broader context of the capital formation goals of Regulation D.

Summary of Comments

1. The Commission's mandate to promote both investor protection and capital formation is promoted by venture capital. We continue to believe that the policy favoring an exemption for venture capital funds from any higher accredited investor standard for PPIVs is appropriate in light of both capital formation and investor protection considerations.
2. The Rule 501 accredited investor standard for issuers generally should be the Regulation D accreditation requirement for venture capital funds. We urge the Commission to ensure that the new flexibility provided in these proposed changes will be available to venture capital firms to the same extent as all other issuers.

² NVCA's comment letter is attached and is also available at <http://www.sec.gov/comments/s7-25-06/jdowling7337.pdf>. (hereinafter the "March Letter").

³ See generally, Michael Halloran, et al., VENTURE CAPITAL AND PRIVATE OFFERING NEGOTIATIONS, Vol. 1 at 3-9 (3rd Edition 2005)

3. The PPIV Release proposal to exempt venture capital from application of the new accredited natural person standard is appropriate and the proposed definition of “venture capital fund” should be modernized to ensure that all venture capital funds are exempted.

4. We support the proposed revisions to Regulation D in this Release that provide greater flexibility for private offerings of securities.

In particular, we support:

- Retention of the current accredited investor standard based on net worth and income
- Addition of the alternative criteria based on investments for qualification as an accredited investor

We also recommend that further consideration be given to reduction of the time lapse required for the Regulation D integration safe harbor to as few as 30 days in the case of an issuer that has shown a clear commitment to a public offering but has withdrawn it because of market conditions.

Detailed Comments

1. The Commission’s mandate to promote both investor protection and capital formation is served by venture capital investing.

Venture capital is a proven success in promoting the capital formation process. For the last four decades, venture capital has helped found and build companies, create jobs, and catalyze innovation in the United States. This contribution has been achieved through long-term investment into small, emerging growth companies across the country and across industry sectors. Venture capital has driven small business capital formation through investments in thousands of US companies per year. Venture capital not only invests in these companies, it helps them succeed and drive economic growth.

According to a study conducted by econometrics firm Global Insight, companies that started with venture capital accounted for 10.4 million jobs and \$2.3 trillion in revenues in the United States in 2006.⁴ According to Global Insight, revenues from venture backed companies represented 17.6 percent of US GDP and 9.1 percent of private sector employment in 2006.⁵ As a whole, these companies created jobs at a rate two and one-half times faster than their non-ventured counterparts from 2003 – 2006 and outperformed non-venture companies in job and revenue growth for every industry sector measured.⁶ Thus nearly one out of every ten private sector jobs is at a company that was originally venture-backed. The fact that almost 18% of US GDP comes from venture-backed companies⁷ is proof of the validity of the venture capital model of capital formation.

Venture investing is also a source of quality economic growth. Capital invested by venture funds has resulted in thousands of successful companies that have pioneered new frontiers. In the biotech sector, venture-backed companies accounted for 54 percent of jobs and 60 percent of revenues in 2006.⁸ Companies that received investment capital from venture funds also accounted for 77 percent of all semiconductor jobs, 88 percent of all jobs in the software industry and 94 percent of all jobs in computer and computer peripherals in 2006.⁹

Venture capital has backed such technology innovations as search engines (Google), computer operating systems (Microsoft), online video sharing (YouTube), and online auctions (eBay). Venture capital has supported life saving medical innovations (pacemakers, ultrasound and various drug therapies). It has supported business model innovations such as superstores

⁴ Testimony of Jonathan Silver, Founder and Managing Director Core Capital Partners, Washington, D.C. before the House of Representatives Committee on Ways and Means, September 6, 2007. Available at <http://www.nvca.org>. For information on prior years, see Global Insight, VENTURE IMPACT, THE ECONOMIC IMPORTANCE OF VENTURE-BACKED COMPANIES TO THE US ECONOMY, (3rd Edition 2007), available at http://www.nvca.org/pdf/NVCA_VentureCapital07.pdf. See generally, 2006 National Venture Capital Association Yearbook, prepared for NVCA by Thomson Financial which includes statistics from the PricewaterhouseCoopers/NVCA MoneyTree™ Report based on data from Thomson Financial.

⁵ *Id.*

⁶ Testimony of Kate D. Mitchell, Managing Director, Scale Venture Partners, Foster City, CA before Senate Committee on Finance, July 11, 2007. Available at <http://www.nvca.org>.

⁷ *Supra* note 3.

⁸ *Supra* note 4.

⁹ *Id.*

(Home Depot and Staples), quality food chains (Whole Foods), and coffee houses (Starbucks). While these companies and innovations are household names today, they were at one time just ideas put forth by unknown entrepreneurs who had little experience in growing a business. The infusion of venture capital dollars and expertise helped turn these ideas into companies. These companies created new markets that have, in turn, fostered the growth of competitors, which have continued the cycle of growth and innovation.

By promoting the strong public policy in favor of job growth, economic development and a higher standard of living for Americans, venture capital supports the Commission's capital formation mission. Therefore, rules that take into account the special role of venture capital in capital formation are completely consistent with the SEC's mission.

Venture capital funds also benefit average investors in many ways. They create operating companies that give public market investors the opportunity to share in significant growth and wealth creation. It is clear that, as much as investors need basic safeguards such as full disclosure, they also need investment opportunities. Literally thousands of companies would not exist today were it not for the venture capital support they received early on. People investing for retirement, to buy a home or to educate their children have benefited greatly from the growth of venture-backed companies like Cisco, Genentech, Outback Steakhouse, Intel, FedEx, Microsoft, Dell, Apple, and the other companies named already in this letter. These companies and many more venture-backed companies have delivered exceptional growth in shareholder value for many years following their initial public offerings and many continue to do so today. Therefore, there is substantial investor benefit that comes from venture capital's focus on taking entrepreneurial ideas to the point of becoming public companies.¹⁰

2. The Rule 501 accredited investor standard for issuers generally should be the Regulation D accreditation requirement for venture capital funds.

¹⁰ In addition, Venture capital funds themselves have collectively delivered above average returns for our country's pre-eminent institutional investors including public pension funds, university scholarship endowments, and charitable foundations.

Under proposed Rules 216 and 509 in the December 2006 PPIV Release a new, higher “accredited natural person” standard would apply for individuals wishing to invest in private pooled investment vehicles such as hedge funds and private equity funds.¹¹ We urge the Commission to give serious consideration to the many comments it received in opposition to this new requirement. Furthermore, and most important, we believe that an exception for venture capital funds from any new requirement is appropriate and fully consistent with the SEC’s mission and the purposes underlying Regulation D. On both capital formation and investor protection grounds stated in our March Letter and in this letter, venture capital funds should not be subject to a higher accredited investor standard than any other private issuers.

There is little if any need for a higher level of sophistication for investors in private placements of venture capital LP interests than for investments in the private placements of private operating companies. The Regulation D Release’s rationale for a new \$2.5 million investments test for investments in PPIVs does not apply and, as the PPIV Release proposed, should not apply in the case of venture capital funds. The Regulation D Release gives several reasons for this higher “accredited natural person” test for PPIV. It says that PPIVs involve “unique risks, including risks of undisclosed conflicts of interest, complex fee structures, and the higher risk that may accompany such vehicles anticipated returns.” Regulation D Release, p. 47-48. To the extent we understand what the Release intends by these various terms, we do not believe any apply to venture capital funds as compared to other private offerings.¹²

Venture investing is straightforward. Venture funds do not rely on leverage, financial engineering or investments in complex securities to produce their returns. Since venture funds focus on investing in operating companies, the risks involved in venture fund investing are the

¹¹ The PPIV Release proposed that a natural person wishing to invest in a PPIV, other than an venture capital fund, would be required to meet the Rule 501 accredited investor standard and, in addition, own not less than \$2.5 million in “investments” as defined under proposed Rule 509.

¹² The language in the Regulation D Release quoted above, regarding “unique risks, including risks of undisclosed conflicts of interest, complex fee structures, and the higher risk that may accompany such vehicles anticipated returns,” appears to come directly from page 17 of the PPIV Release. Footnote 42 on page 17 of the PPIV Release cites the 2003 SEC Staff Study of Hedge Funds in support of the statement that private investment pools “have become increasingly complex and involve risks not generally associated with many other issuers of securities.” Since the 2003 Hedge Fund Study found no basis to recommend change in regulation of venture capital funds, there appears to be no factual basis nor a regulatory rationale in either this Release or the PPIV Release for applying a heightened accredited investor standard to venture capital funds.

and GP interests. This alignment obviates any need for heightened investor protection based on “undisclosed conflicts of interest.”

Therefore, none of the stated reasons in the Regulation D Release, or the PPIV Release,¹⁴ for establishing a higher PPIV investor qualification standard apply to venture capital. As such, it is appropriate to treat venture capital funds the same as other private issuers.

3. The PPIV Release proposal to exempt venture capital from application of the accredited natural person standard is appropriate and the proposed definition of “venture capital fund” should be modernized to ensure that all venture capital funds are exempted.

As noted already, the Commission’s capital formation mandate and the more targeted purpose of Regulation D form a sound policy basis for the treatment of venture capital funds in the same way as other private issuers. Therefore the PPIV Release made an appropriate distinction when it exempted venture capital funds from any heightened standard for private pooled investment vehicles. Not only is the determination appropriate, it is necessary in order to preserve a key ingredient in the success of venture capital funds.

As stated more fully in NVCA’s March Letter commenting on the PPIV Release, the vast majority of the capital for venture funds comes from institutional investors that meet Rule 501 standards other than the standard for “natural persons,” i.e., individuals. However, the availability of the current Rule 501 accredited investor standard for individuals is critical to the success of venture investing. An accredited investor standard for individuals higher than the current standard would eliminate the ability of some scientists, engineers, academics, entrepreneurs and other “Network Individuals” to invest in venture capital funds. This would eliminate a critical incentive for these key players to assist in the identification and development of investment opportunities for the benefit of the venture fund. Our March Letter provides more

¹⁴ *Supra* note 12.

4. We support the proposed revisions to the limited offering exemptions in the Regulation D Release that provide greater flexibility for private offerings of securities.

As noted above, we support retention of the current accredited investor standard for Regulation D offerings. This definition has served both venture funds and their investors well. We support the Regulation D Release proposal to add an alternative means of qualifying accredited investors based on investments only. While we cannot predict how much this test will be used in lieu of the income or net worth tests in Rule 501, the criteria is as rational as the income and net worth tests in place and should allow greater flexibility for both funds and investors. We do believe however, that a simpler, or a more principle-based definition of "investment" would make the new criterion more useful and could help promote reliance on that standard.

In keeping with the intent of the Regulation D Release, we recommend that the Commission give further consideration to reducing the period of time for application of the integration safe harbor.²⁰ We are particularly concerned with at least one circumstance.

The key event in the life of many successful venture backed companies is the initial public offering. Of course, the market for IPOs is notoriously unpredictable. It is not uncommon for a company to make a full commitment to a public offering and still be required to stop short of completing the offering because of a change in market conditions. When this occurs, an excellent company can suddenly become very fragile in a number of ways. The ability to access the private market for capital within thirty days of the abandonment of an IPO could enhance the prospects for such a company's continued success. On the other hand, denial of new private capital for even ninety days, as is proposed in the Regulation D Release, could increase the vulnerability of the company. Therefore, we recommend that consideration be given to shortening the integration period to thirty days in at least the circumstances described here in

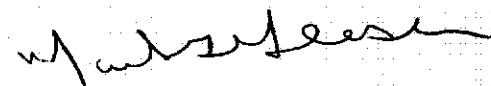
²⁰ The SEC Small Companies Advisory Committee recommended that the time lapse applicable to the integration safe harbor be reduced to 30 days for all offerings. Final Report of the Advisory Committee on Smaller Public Companies, (April 23, 2006), pages 94-96.

order to provide clarity and certainty for issuers that find themselves in this difficult situation.²¹
We are aware that there are concerns regarding abuse of such a rule and would be pleased to assist the staff in developing language to cover this situation while minimizing the risk of abuse.

Conclusion

NVCA appreciates the Commission's efforts to improve the flexibility of Regulation D. We also appreciate the Commission's recognition that venture capital funds play an important role in fostering the goals of Regulation D and should, therefore, be exempt from any heightened accredited investor standard that might be established for private pooled investment vehicles. We appreciate your consideration of our comments and recommendations. If we can be of further assistance in regard to any of these matters, please contact me or Jennifer Connell Dowling, vice president for federal policy at 703 524 2549.

Very Truly Yours,



President

²¹ We understand that the Commission attempted to address the problem of a withdrawn public offering in 2001 through Rule 155(c); however, a simpler integration Rule would be far more effective in promoting capital formation in this situation. *See generally*, Charles J. Johnson & Joseph McLaughlin, CORPORATE FINANCE & THE SECURITIES LAWS, (3rd Edition, 2004), pages 549-553.



Nancy M. Morris
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549

**Re: Comments on Proposed Rules:
Prohibition of Fraud by Advisers to Certain Pooled Investment
Vehicles; Accredited Investors in Certain Private Investment Vehicles
Release No. 33-8766; IA-2576; File No. S7-25-06 (the "Proposed
Rules")**

Dear Ms. Morris:

We are pleased to have the opportunity to comment on the Proposed Rules, with a specific focus upon the Proposed Rules' impact on the venture capital industry.

The National Venture Capital Association represents approximately 450 venture capital and private equity firms. In this capacity, we seek to communicate the public policy interests of the venture capital community, promote and maintain high professional standards, provide reliable industry data, sponsor professional development, and facilitate productive interactions among our members.

Summary of Principal Conclusions

1. The Proposed Rules appropriately exclude venture capital funds from the new requirement that a natural person have at least \$2.5 million in investments to qualify as an accredited investor (the "New Accredited Investor Rule"). Venture capital funds rely upon broad networks of individual scientists, engineers, academics, entrepreneurs and others ("Network Individuals") to assist in the identification and development of portfolio companies. Allowing Network Individuals to invest in venture capital funds is an important method by which these individuals are incentivized to apply their talents for the benefit of the funds and their portfolio companies. Because many Network Individuals lack the personal wealth to make and hold \$2.5 million in investments, application of the New Accredited Investor Rule to venture capital funds would disrupt this incentive mechanism and thereby impair the functioning of the venture capital industry.

2. The definition of "venture capital fund" contained in the Proposed Rules (i) is extremely complex and (ii) as a result of recent trends in the industry, fails to capture many true "venture capital" funds. If this definition were not corrected, the New Accredited Investor Rule would apply with respect to a substantial and growing number