

THE UNITED STATES SECURITIES AND EXCHANGE COMMISSION

ADVISORY COMMITTEE ON SMALL AND
EMERGING COMPANIES MEETING

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Securities and Exchange Commission
100 F Street, NE
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MR. GRAHAM: So welcome everyone to today's meeting of the Advisory Committee on Small and Emerging Companies. And a special welcome to Mike Pieciak. Hello, Mike.

MR. PIECIAK: Thank you.

MR. GRAHAM: Who is the Deputy Commissioner of Vermont Securities Division and he is here as the committee's representative from NASAA, which is North American Securities Administration Association -- Administrator's Association.

And we very much appreciate you're being here and look forward to the kinds of insights that your experience gives you.

We have a full agenda for today as we delve into a timely topic of secondary market liquidity. Secondary market liquidity has always important to the overall success of private companies, but increasingly as companies remain private longer than in the past this topic is of growing importance when talking about the ability of private companies to raise capital. It is also a critical issue in connection with publicly issued securities of those small and emerging companies who have difficulty attracting the attention of investors and market makers.

1 We understand that a number of you have these
2 issues that are under consideration right now by the
3 Commission that it seems particularly important for our
4 committee to pick this up. To help frame our discussions
5 today we have a range of presentations from Annmarie
6 Tierney, Vincent Molinari and David Weild. And I don't
7 know if any of you are here at the moment -- Vincent?

8 MR. MOLINARI: Yes, sir.

9 MR. GRAHAM: Okay. Good morning. So we will
10 hear from you this afternoon and thanks for being here.

11 But before we go any further, Chris, you want
12 to acknowledge --

13 MS. JACOBS: Yes.

14 MR. GRAHAM: -- Chair White and others.

15 MS. JACOBS: I want to echo Stephen's good
16 morning. But before we continue I would -- and turn the
17 floor over to Chair White, I would like to speak for the
18 committee or speak on behalf of the committee and say
19 thank you to Chair White and the commissioners for
20 attending this morning, but more importantly giving us a
21 forum with which we can opine or give voice to the issues
22 that are so pertinent to us today, which is capital
23 formation, support of our small companies, and our
24 startups. So with that thank you again and good morning.

25 CHAIR WHITE: Good morning. And thank you,

1 Chairs and Steve as well. Good morning everybody. Thank
2 you all for being here. I'll be very brief so you can
3 get down to business, your business at hand. I'm really
4 in listening mode today.

5 I would, though, like to also welcome Michael
6 Pieciak who will add really invaluable knowledge to this
7 committee's work. So welcome, Mike.

8 And today's agenda, as is always the case with
9 this committee, addresses several important topics
10 including Regulation A+ as we call it, secondary market
11 liquidity, and recommendations regarding the definition
12 of accredited investor. And as Steve said all of those
13 issues are quite timely topics for the Commission's
14 currently ongoing work in these areas.

15 As you know Regulation A+ and crowd funding
16 rule makings are designed to facilitate smaller
17 companies' abilities to access capital and to provide
18 investors with additional investment opportunities. In
19 making investment decisions investors may naturally
20 consider whether they will have the ability to resell
21 their shares in the future. I mean, there's simply no
22 doubt that secondary market liquidity is an important
23 factor impacting the availability of capital for small
24 businesses as well investor protection.

25 SEC staff in the Division of Corporation

1 Finance and Trading in Markets have been looking at
2 various means to facilitate the secondary market trading
3 of securities issues by small businesses. Among a number
4 of other possible avenues the staff is considering
5 whether the development of appropriately structured
6 venture exchanges could provide more liquidity for the
7 securities of smaller companies. Some earlier exchanges
8 have not been successful. Obviously the reasons for that
9 need to be carefully studied along with other issues.
10 Smaller companies are important to our economy and
11 it's important to support appropriately a market
12 structure that promotes the capital formation of smaller
13 companies while providing robust investor protections.
14 And more generally as I've emphasized on several
15 occasions one market structure may not fit all and the
16 Commission must concretely focus on how to enhance the
17 market structure for small companies.

18 I look forward to perspectives and ideas from
19 your committee on what obstacles and possible solutions
20 you see to the development of secondary market liquidity
21 venues for privately issued securities. So as promised I
22 will be brief, stop, let you get down to business.
23 As always we very much appreciate your expertise
24 and efforts. Facilitating small business capital
25 formation is a priority we all share and it is our job

1 with your help to convert the supportive words into
2 workable and effective actions. Thank you very much.

3 MR. GRAHAM: Thank you. Commissioner Gallagher
4 -- Aguilar.

5 MR. AGUILAR: I'm easy. You know, I'm easy to
6 forget. I always have to thank Dan Gallagher for
7 recognizing that I am a commissioner and more senior to
8 him.

9 MR. GALLAGHER: I just feel he's always looking
10 over my shoulder.

11 MR. AGUILAR: That's a good head to be on. But
12 thank you and good morning to everyone, and my thanks to
13 Dan for letting me speak now.

14 I want to start by welcoming the members of the
15 Advisory Committee on Small and Emerging Markets. I
16 truly appreciate your efforts and look forward to today's
17 discussion. I also want to thank the staff at the
18 Division of Corporation Finance, Office of Small Business
19 Policy for organizing this meeting.

20 In the interest of time I'll make some brief
21 remarks this morning, but perhaps not as brief as Chair
22 White. But I'll put a more fulsome set of remarks on the
23 SEC's website that contains more details about my
24 thoughts and Noble 33 footnotes for additional
25 information.

1 I'm delighted to see that today's meeting will
2 discuss the secondary trading environment for the
3 securities of small business. The lack of a fair, liquid
4 and transparent secondary market for these securities is
5 a long standing problem that needs an effective solution.

6 The topic is increasingly urgent in light of certain new
7 or anticipated Commission rules required by the JOBS Act
8 that result in a far wider range of small business
9 securities needing to find liquidity in the secondary
10 markets.

11 Specifically, proposed rules under Regulation
12 A+ and crowd funding and final rules under Rule 506(c) of
13 Regulation D would permit wide distribution of securities
14 and would also allow such securities to be freely traded
15 by security holders immediately upon issuance or after a
16 one year holding period. These registration exemptions
17 also provide or are expected to provide for lesser
18 ongoing reporting requirements that is required for
19 traditional listed securities.

20 Moreover, under the Commission's recently
21 proposed rules to amend Section 12(G) of the Exchange Act
22 as required by the JOBS Act, the number of record holders
23 a company may have before it is required to publish
24 annual and quarterly reports would greatly increase. The
25 end result is that companies would be able to sell their

1 securities to a wider swath of the public and remain
2 outside of the protections of the Exchange Act for longer
3 periods of time, perhaps even permanently. As a result,
4 investors who acquire these shares, many who are expected
5 to be less financially sophisticated, may be left holding
6 shares that they are unable to sell.

7 Now one idea that has been suggested as a way
8 to foster an active secondary market for small company
9 stocks is for the Commission to approve one or more
10 venture exchanges. Such exchanges would be limited to
11 smaller cap companies that are expected to meet less
12 stringent listing standards. Clearly the common anomaly
13 of unregistered and unlisted shares requires some new
14 solutions and venture exchanges may be a viable
15 alternative.

16 Venture exchanges are hardly a new idea however,
17 and prior efforts to establish them in this country have
18 fared poorly. Accordingly, we need a thoughtful and
19 prudent approach that carefully examines why the prior
20 attempts failed. For example, we should carefully
21 examine the reasons for the demise of the American Stock
22 Exchange Emerging Company Marketplace, known as ECM.
23 Although the ECM's lower transaction costs allowed it
24 to thrive for a time the exchange eventually succumbed to a
25 number of serious design flaws.

1 For instance the proper forum to join the ECM
2 eventually graduated to the American Stock Exchange.
3 This created the impression that the ECM was populated
4 only by unsuccessful companies. The ECM's image problem
5 was made only worse by the exchange's failure to properly
6 screen candidate firms and the scandals involving some
7 ECM companies only cemented the exchange's reputation as
8 a lawless wild west.

9 Finally, one academic study suggested the lower
10 bid and ask spreads that prevailed on the ECM may have
11 dissuaded broker/dealers from making markets for those
12 stocks, which may have decreased liquidity. It may have
13 also deterred broker/dealers from distributing research
14 on these companies.

15 The issues raised by ECM's demise are both
16 complex and interrelated. But it is not the only source
17 of guidance available to us. There have been other
18 attempts to create viable markets for smaller companies.

19 For example, many European stock markets have
20 experimented with a junior exchange for companies too
21 small to meet normal listing standards. These efforts
22 unfortunately generally have been unsuccessful and we
23 should try to understand why.

24 Moreover, NASDAQ's efforts in 2011 to establish
25 a new venture exchange in the United States appears to

1 have stalled. We should understand why that has occurred
2 as well.

3 Finally, we should examine the recent struggles
4 of Canada's TSX Venture Exchange. It is reported that
5 TSX's over reliance on mining and energy firms has left
6 that exchange in the midst of a crisis due to the global
7 collapse in commodity prices. So we need to explore the
8 appropriate diversity of the companies that go on any
9 venture exchange.

10 In addition, it's been reported venture
11 exchanges both here and abroad have suffered from low
12 liquidity and at times high volatility. This means
13 investors could lose a lot of money quickly and could
14 have trouble selling their shares in the downturn. The
15 Commission should attempt to determine the underlying
16 causes of these problems and how best to address them,
17 and in this regard we may need to ask some difficult
18 questions.

19 For example, should venture exchanges be
20 structured as dealer markets rather than auction markets?
21 Also could venture exchanges enhance liquidity through
22 batch trading rather than continuous trading? How can
23 the Commission consistent with the Exchange Act encourage
24 traders to execute transactions on venture exchanges
25 rather than in off exchange venues? And finally could

1 larger tick sizes enhance liquidity by encouraging market
2 maker activity and fostering research? In this regard
3 the Commission's proposed tick size pilot program may
4 offer valuable insights on the role of tick sizes in
5 ensuring an active secondary market for smaller
6 companies.

7 Importantly, each of these questions presents a
8 possibility of a tradeoff between what is best for
9 investors and what is best for the exchange and its
10 participating broker/dealers. We must be mindful of
11 these tradeoffs as we review any proposal for new venture
12 exchanges.

13 We must also never lose sight of our core
14 responsibility, which is to protect investors above all
15 else. To be sure venture exchanges can and do attract
16 reputable and profitable companies, but experience has
17 shown that venture exchanges and the companies they list
18 may present more risk than investors realize. The
19 commissioners need to understand how best to address
20 these risks before approving more of these exchanges. It
21 also needs to make certain that investors understand
22 these risks.

23 Those who have studied venture exchanges
24 believe that they are far more likely to succeed when
25 they focus on investor protection and education. Venture

1 exchanges that implement appropriate listing standards
2 and enforce them conscientiously and educate investors
3 about the higher risks involved with small cap companies
4 seem to do better. Those that have not have struggled.

5 In addition, experts have pointed to other
6 factors that can improve venture exchanges' performance.

7 For example several academics have argued that some
8 listing standards are more important than others. These
9 experts have asserted that while it may be appropriate
10 for venture exchanges to lower certain listing standards,
11 such as minimum firm size, other standards should be
12 inviolate. In particular these experts believe that
13 effective corporate governance standards and accounting
14 requirements are essential to the viability of any
15 venture exchange.

16 In sum, venture exchanges are a possible
17 solution to a looming problem and need to be seriously
18 considered. We should do so in a thoughtful and measured
19 manner, fully cognizant of benefits causing challenges
20 and always with the needs of investors at the forefront.

21 Now another measure that I know the committee
22 is not going to discuss today but I wish you would at
23 some point is to consider to facilitate secondary trading
24 in small business securities, is to revise and update
25 Exchange Act Rule 15c2-11 and its so-called piggyback

1 exception. Rule 15c2-11 is widely used by broker/dealers
2 who trade in unlisted securities.

3 Now in order to use Rule 15c2-11 broker/dealers
4 who wish to publish or quote unlisted securities, which
5 would often be smaller issuers, are required to review
6 and maintain certain information about the security and
7 the issuer. In addition, Rule 15c2-11 requires
8 broker/dealers prior to publishing quotes of these
9 unlisted securities to have a reasonable basis for
10 believing that this information is accurate in all
11 material respects and that it was obtained from reliable
12 sources.

13 In this way Rule 15c2-11 is about trust.
14 Specifically investors need to have confidence that the
15 quotes for these securities are fair and accurate.
16 Without this confidence a fair and liquid secondary
17 market for these securities will not exist. In this
18 regard the use of current Rule 15c2-11 often fails to
19 meet expectations of fair and accurate pricing and often
20 fails to result in reliable quotes.

21 Most critically under the Rule's piggyback
22 exception broker/dealers are permitted to public
23 quotations for a security without complying with the
24 Rule's information requirements if any other
25 broker/dealer has published regular and frequent

1 quotations for that security.

2 As a result broker/dealers need not review the
3 information collected and reviewed by the other
4 broker/dealers before publishing their own quote.
5 Moreover, because the exception allows broker/dealers
6 simply to rely on their own prior quotations
7 broker/dealers have no obligation to confirm that the
8 information they initially relied on when they first
9 published a quotation is still valid no matter how old
10 the initial quotation is.

11 The problems with Rule 15c2-11 have long been
12 recognized. In fact back in 1998 and again in 1999 the
13 Commission proposed comprehensive amendments to Rule
14 15c2-11 to address concerns about fraud and manipulation
15 that had become increasingly common in micro-cap
16 securities traded in the over the counter markets.

17 Many of the concerns raised by these proposed
18 amendments are equally applicable to today's secondary
19 market for small business shares, including, one,
20 eliminating or amending the broker/dealer piggyback
21 exception for small business securities. This would
22 require broker/dealers that wish to publish quotations to
23 conduct a review of issuer and security information and
24 not simply rely on the work of other broker/dealers or
25 their own stale review; two, requiring broker/dealers

1 that publish quotations to obtain and review current
2 information about an issuer at least annually if not more
3 frequently; and three, enhancing investor access to the
4 information collected, reviewed and maintained by the
5 broker/dealer about the issuer. This information could
6 be made easily available to investors over the Internet.

7 In addition of course it would be critical to
8 update Rule 15c2-11 to take into account the new
9 information and filing requirements that are expected to
10 be required under Reg A+ and crowd funding. I think
11 15c2-11 needs to be brought into the 21st century and I
12 think this committee and others should take a hard look
13 at it.

14 Before I conclude I also want to note that you
15 will be considering recommendations on the accredited
16 investor definition. That's a topic I've discussed with
17 this committee back in December 2014, just a few months
18 ago, and my views remain the same so I'll add nothing this
19 morning.

20 I also wanted to acknowledge another topic that
21 you're going to discuss today, which is the so-called
22 Rule 4(a)(1-1/2) exemption. As shareholders rely on this
23 exemption to sell their restricted securities in a
24 private transaction without being considered an issuer or
25 an underwriter, I welcome the Commission's view on

1 formalizing Rule 4(a)(1-1/2) but I acknowledge that it
2 doesn't solve the basic problem of whether a seller will
3 be able to find a willing buyer or access a secondary
4 trading market that will be fair, transparent and liquid.

5 For the latter to occur we will need much more than
6 simply clarifying the contours of Rule 4(a)(1-1/2).

7 Ultimately the goal is to develop a viable
8 secondary trading environment that promotes a fair,
9 transparent and liquid market for the securities of small
10 businesses. I look forward to a robust discussion and
11 any and all viable suggestions as to how to improve the
12 secondary trading environment for shares of small
13 business securities.

14 I thank you for your time and I thank you
15 really for your work and your dedication. And no more --
16 no more from me this morning.

17 MR. GRAHAM: Thank you, Commissioner Aguilar.
18 Is it okay for Commissioner to Gallagher to speak now?

19 MR. AGUILAR: Yes, he has my permission.

20 MR. GRAHAM: All right.

21 MR. GALLAGHER: Well, we're going to have to
22 amend my remarks before we post them to thank
23 Commissioner Aguilar for that because they thank Chris
24 and Stephen right now but --

25 Thank you very much and thanks in particular to

1 the Division of Corporation Finance's Office of Small
2 Business Policy of organizing today's meeting.
3 As I said to Sebastian and Keith before the
4 meeting, I think Sebastian is the hardest working man
5 certainly in the building, maybe in Washington, not that
6 that's the highest standard to meet. But thank you for
7 all you do, Sebastian. You do a great job.

8 CHAIR WHITE: You say the hardest working man
9 in the building? Just --

10 (Laughter.)

11 MR. GALLAGHER: Touché. Touché. Well played,
12 well played. No further comment there.

13 And of course a special thank you to the
14 committee members. Again I've been impressed, really
15 impressed by your willingness as a very important and
16 recently reinvigorated committee to jump right in and
17 tackle a very substantive agenda at the outset. So thank
18 you very much for that.

19 And I'm sure it will come as no surprise to you
20 that I was absolutely thrilled to see the committee
21 taking up the vitally important issue of secondary
22 liquidity in the areas of small and emerging growth
23 companies. As most of you know this is an issue that I
24 have been pounding the table on for years because
25 secondary trading of course implicates all three prongs

1 of the SEC's tripartite mission to protect investors,
2 maintain fair and orderly and efficient markets, and
3 importantly facilitate, active verb, capital formation.

4 And if the Commission takes steps to enhance
5 these markets we will make them more fair and efficient.

6 We can increase the ability of an investor to exit
7 his or her investment in these markets and decrease the
8 illiquidity discount of the investment, and we can
9 enhance oversight and transparency into issuers, thereby
10 promoting investor protection. And that in turn will
11 increase investors willingness to participate in the
12 primary issuance of securities, which enhances capital
13 formation for these companies that are a lifeblood to our
14 economy.

15 As I noted in a speech at The Heritage
16 Foundation last September, the SEC needs positive,
17 proactive capital formation agenda for small businesses
18 that encompasses all phases of growth in both the private
19 and public markets, and today the committee is discussing
20 two pieces of that agenda. First it will focus on
21 enhancing secondary trading in private shares both in
22 general and through a focus on Rule 4(1-1/2), and if
23 greater certainty in this area for example through
24 Commission guidance would help participants in these
25 markets then we should make that a priority. So I look

1 forward to hearing your take on these
2 issues.

3 Second, the committee will examine secondary
4 market trading of small company shares, particularly
5 through venture exchanges. I believe venture exchanges
6 are a vital bookend to our JOBS Act rulemaking on Reg A+.
7 And in thinking about these entities I've been
8 envisioning them as national securities exchanges with
9 full state law preemption, but with tailored periodic
10 reporting and listing requirements that are more
11 appropriate for small business. They would be exempt
12 from the national market system rules and the uniform
13 trading privilege requirements so as to concentrate
14 liquidity in the listing venue and would be free to
15 structure trading however they see fit, for example
16 periodic auctions instead of continuous trading.

17 I believe these principles would create
18 liquidity in Reg A+ shares, and moreover these same
19 principles could be extended to the shares of the
20 smallest public companies currently traded over the
21 counter to facilitate liquidity for them as well.

22 We must embrace change and we must depart from
23 the failed policies and feeble ideas of the past in order
24 to pursue critically needed innovation like venture
25 exchanges. I believe this Commission has the courage and

1 leadership to do so. So needless to say I'm very excited
2 to listen to the discussion today and I'll stop there so
3 that we can get to the discussion even faster. So thanks
4 again to everyone for participating.

5 MR. GRAHAM: Okay, thank you. And Commissioner
6 Piwowar.

7 MR. PIWOWAR: Oh, very good. Thank you,
8 Stephen.

9 I want to thank you and Chris for your
10 continuing leadership as co-chairs of the committee,
11 something I look forward to, being able to engage with
12 you all every time you come to town here. I want to
13 thank all the members of the committee for being here,
14 taking your time to be with us today. In particular I
15 want to welcome Mike Pieciak. Although it many get
16 confusing by having Mike Pieciak and a Mike Piwowar at
17 the same table we'll see what we can do.

18 I also want to thank the staff for their
19 support of the committee's activities. Today's meeting
20 will focus on a number of important topics to the small
21 business community. I look forward to the committee's
22 recommendations on regulation D's -- Reg D's definition
23 of accredited investor, a definition that has been widely
24 criticized for being under inclusive as well as the
25 discussion about Reg A+ offerings, an important provision

1 of the JOBS Act that we need to implement without further
2 delay.

3 Most importantly I look forward to the
4 presentations and discussions on secondary market
5 liquidity. Not only does greater liquidity translate to
6 lower trading costs for investors, numerous academic
7 studies have shown that increases in a company's -- in
8 the liquidity of a company's stocks and bonds can reduce
9 its cost of capital and increase its market value. Lower
10 cost of capital translates into more opportunities for
11 investment, innovation, creativity and ultimately jobs.

12 This is particularly important for small
13 businesses. A recent Harvard business school working
14 paper estimates that small businesses have created
15 approximately two-thirds of all new net jobs in this
16 country since 1995. Unfortunately small businesses were
17 hit harder than larger businesses from the recent
18 recession and have found it more difficult to get bank
19 based financing during the current tepid recovery.

20 While the Dodd Frank Act was touted as being
21 focused on Wall Street financial firms at the epicenter
22 of the financial crisis, the costs of the law and the
23 regulations that have followed have been
24 disproportionately born by main street businesses that
25 had absolutely nothing to do with the financial crisis.

1 Bank based financing has become so costly and so
2 politicized that small businesses must look elsewhere.
3 That is why it is so critical that we, collectively we,
4 the Commission and the committee, continue to work
5 together to find ways to improve access to capital
6 markets based financing by small businesses.

7 Thank you again for volunteering your time and
8 thank you again for all your efforts spent as part of
9 this important committee.

10 MR. GRAHAM: Thank you, Commissioner.
11 Commissioner Stein wanted to be here today but she's
12 traveling, so she sends her regrets and she also sends
13 her thanks to you all.

14 Let's move on to Keith Higgins. We would like
15 to introduce Keith. I think all of you know who Keith
16 is. He's the director of the Division of Corporation
17 Finance and Keith will also introduce the rest of the SEC
18 staff with us this morning.

19 MR. HIGGINS: Thanks Stephen and Christine.
20 Good morning. I would like to add my welcome to everyone
21 here today and to thank you from the division for
22 bringing your experience, your expertise and your
23 insights today to share with the Commission and the
24 public.

25 The issues that you'll be addressing today are

1 extremely current and they're very important to the
2 division. They are things that were are currently and
3 actively working on. I'm personally and I know the
4 others here are very interested in the presentations and
5 in your discussion today and they'll inform the work that
6 we do ahead.

7 I would like to introduce people who probably
8 need no introduction, but to my right is Sebastian Gomez
9 Abero who is the chief of the office of small business
10 policy. Julie Davis is the senior special counsel in the
11 office, and as you know in addition to working with the
12 committee the Office of Small Business Policy is really
13 the Commission's portal to the small business community
14 and actively works with small businesses to help in
15 capital formation and other matters.

16 Before getting started I would like to give the
17 obligatory disclaimer that anything that the three of us
18 say today will represent our own views and don't
19 represent the views of the Commission or any other member
20 of the staff. And with that I would like to turn it back
21 to the Christine and Stephen to lead the discussion on
22 the accredited investor definition.

23 MR. GRAHAM: All right. Thank you. And
24 welcome John. I see that you made it. It's oftentimes -
25 - there's always some one of us who has had an adventure

1 in travel. But it's nice that you made it.

2 MR. HEMPILL: My flight got cancelled as well
3 so --

4 MR. GRAHAM: Oh, really? Well, if I can give
5 you one piece of advice don't hitch a ride with Catherine
6 because her car breaks down.

7 Okay. It's on to the recommendation on the
8 accredited investor definition. As those of you who
9 attended the last meeting remember we approved a set of
10 recommendations relating to the definition of accredited
11 investor. Between that meeting and this meeting we've
12 had an opportunity to put pen to paper to kind of capture
13 everyone's thoughts. I believe that the -- that the
14 recommendations that you all have received reflect what
15 was agreed to, and so therefore I would like to ask for a
16 motion that the we adopt these recommendations.

17 A PARTICIPANT: So moved.

18 MR. GRAHAM: Can I get a second?

19 A PARTICIPANT: Second.

20 MR. GRAHAM: Okay. Any further discussion?
21 Sarah?

22 MS. HANKS: Yes. Could we discuss a couple of
23 wording changes?

24 MR. GRAHAM: Yes.

25 MS. HANKS: Because we didn't have -- okay.

1 MR. GRAHAM: Yes.

2 MS. HANKS: In recommendation 8 we use the word
3 laudable for the underlying premise that retirement
4 assets should be treated differently. I suggest that we
5 remove the word laudable and use the word understandable
6 instead. We don't want to encourage a particular tax
7 treatment to result in a different result with respect to
8 whether assets are included or not included in the
9 definition.

10 MR. GRAHAM: Okay.

11 MS. HANKS: And the other wording change along
12 similar lines in recommendation number 1 that we use the
13 words -- that we add the words tax treatment of assets
14 included in net worth should be disregarded.

15 MR. GRAHAM: I'm sorry, what was that again
16 please?

17 MS. HANKS: Yes. That's recommendation number
18 1. At the end or wherever you would like to put it the
19 words tax treatment of assets included in net worth
20 should be disregarded or you can have something --

21 MR. GRAHAM: Tax treatment --

22 MS. HANKS: What I'm trying to get at is the
23 fact that something is a retirement asset or it has a
24 different -- it's in a 401(k) or not should play no role
25 in whether something is treated as an asset in the

1 calculation. I'm certainly open to different wording.

2 MR. GRAHAM: Yes, it's -- I appreciate the
3 thought and I think that that's consistent with what we
4 have here. I'm just wondering if that's clear and if it's
5 required even.

6 MS. HANKS: I'm certainly -- I'm certainly not
7 going to force that. But the one wording change I think
8 that we do need to change is laudable.

9 MR. GRAHAM: That makes sense to me. DJ?

10 MR. PAUL: Yes, and the rationale for the --
11 sorry. Thank you. The rationale for adding the verbiage
12 that -- for the first recommendation is in the -- to keep
13 things simple in the event that there is some sort of tax
14 change in the future over time so it doesn't become
15 overly complicated, is that where you're headed or what
16 is --

17 MS. HANKS: Just because it should play no role
18 in whether something is traded is an asset or not. How
19 it's treated as a -- under the tax code is irrelevant in
20 determining whether it's an asset or not.

21 MR. GRAHAM: And I don't disagree with that.

22 MS. HANKS: Thank you. I mean you might think
23 that it's implicit in the recommendations but I thought
24 making it explicit would be useful.

25 MR. GRAHAM: Because we -- do we hit that with

1 the last bulletin 8 or even --

2 MS. HANKS: It does become implicit but the
3 problem is that it's not actually included in the
4 recommendations.

5 MR. GRAHAM: Okay. I don't -- well, let me
6 open it up. Comments? I personally have no issue with
7 making that clearer because I think the point is that the
8 tax treatment shouldn't be a factor in terms of -- the
9 tax treatment of a particular asset shouldn't be a factor
10 in determining whether or not somebody achieves
11 accredited investor status.

12 So I think -- I think we can all agree with
13 that concept. We'll find the right language.

14 Any other comments? Okay, with those changes
15 all those in favor.

16 (Chorus of ayes.)

17 MR. GRAHAM: Any opposed? Any abstentions?
18 We're done. Thank you.

19 Okay. Onto Regulation A+ and the issue of
20 state preemption. I think we all know that the
21 Commission is working hard to finalize the amendments to
22 Regulation A and many are eagerly anticipating this
23 rulemaking as it has the potential to be a robust capital
24 raising tool. One of the primary debates on this issue
25 has surrounded the question of state preemption, and that

1 is whether the issuers will need to register and qualify
2 these offerings with state securities regulators as well
3 as with the SEC.

4 To help tee up our discussion we've asked DJ
5 Paul and Mike Pieciak to give us some opening commentary.

6 So DJ do you want to start? Okay, Michael, go for it.

7 MR. PIECIAK: All right, well thank you, DJ.
8 That's very gracious of you and I'm sure we'll probably
9 have the same things to say anyway.

10 Well, I think it's actually appropriate that I
11 start because I did want to provide some background on
12 Regulation A and just give sort of the context of what
13 we're talking about. I had dinner with a friend in New
14 York City on Monday night and I told him I was talking
15 about Regulation -- or Reg A today and he thought it was
16 Bob Marley or something like that. So I think it's
17 probably helpful to sort of give an overview of what
18 we're even talking about.

19 So Regulation A is an exemption from full blown
20 registration at the SEC. It's sort of a mini
21 registration process. As we live in a dual regulatory
22 world of state and federal regulation there's also
23 regulation at the state level when businesses do
24 Regulation A filings. The process that they use at the
25 state level in the past had been registration by

1 qualification. So that was sort of the framework for
2 Regulation A.

3 In the 1990's there were sort of a high mark of
4 Regulation A activity. There were about 117 offerings in
5 1997. That number went down to more about 40 offerings
6 in the 2000's, and then we see in 2011 that there were
7 only about 19 offerings conducted or filed I should say
8 with the SEC under Regulation A.

9 So the question really was why is Regulation A
10 underutilized. And there was a GAO study that looked
11 into this and identified really four main factors as to
12 why Regulation A had declined so dramatically from 1997
13 to today. The first was that there was another exemption,
14 Regulation D 506, that was quite prevalent. You don't
15 have to file with the SEC except for a notice filing.
16 You don't have to file with the states except for a
17 notice filing where you have sales in those states.

18 So that was a big benefit to issuers they
19 found. Also there's no limit. The limit on Regulation
20 A filings is \$5 million, or was. There's no limit under
21 Regulation D. The report also found that the timeframe
22 with -- complying with the SEC registration was long and
23 sometimes undefined and difficult to comply with.
24 Similarly they found that compliance with state Blue Sky
25 laws was difficult in terms of the research of which

1 state laws were applicable, which states you were filing
2 in, and that onus the was on the small business issuer.

3 And then lastly they found that the cap was too
4 low at \$5 million. The last time the cap had been raised
5 was 1992, and obviously it's a different world now than
6 it was 1992.

7 So under the JOBS Act the Congress went to work
8 to identify some, you know to fix some of these issues,
9 most obvious being raising the cap from \$5 million to \$50
10 million under the Tier 2 offerings, what's now as Reg A+
11 offerings. Reg A+ offerings also are going to be
12 considered covered securities, which means that similar
13 to 506 Reg D offerings they're preempted by state action
14 when they're traded on the national exchange and when
15 they're so-called purchased by qualified purchasers.

16 So what the issue really is here today is what
17 the definition of that qualified purchaser is. NASAA,
18 the North American State Securities Administrators
19 Association, has laid out in great detail their legal
20 arguments as to why we think qualified purchaser as the
21 SEC has defined it or proposed to define it is outside
22 the congressional intent of what the JOBS Act intended.
23 That the plain meaning of the word of the statute -- and
24 I probably should even backtrack and say that the SEC has
25 decided or has proposed to define qualified purchaser as

1 anyone that purchases a Regulation A+ offering. So
2 essentially it would be anyone that purchases the
3 Regulation A offering instead of some sort of subset of
4 that group. But, you know, the thing I did not want to
5 focus on was necessarily our legal arguments, which we
6 think are sound, but I wanted to focus on was a very
7 exciting program that NASAA undertook in the fall of 2012
8 which is relating to this handout that I passed out or
9 that Julie passed out, thank you, just a moment ago,
10 which is the NASAA coordinator review program.

11 So there really is a new day among state
12 regulators in terms of capital formation initiatives and
13 capital formation innovation and ideas, and Regulation A
14 coordinated review is a great example of that. Under
15 coordinated review the onus that I mentioned and the GAO
16 report mentioned of having to do research into individual
17 states and then comply with individual state comment
18 letters has gone away because there is now one single
19 state that you communicate with and the states regularly
20 communicate among themselves in terms of what the
21 comments are going to be to a Regulation A offering and
22 work among themselves to smooth out any inconsistencies
23 in the comment letters and provide really a streamlined
24 service to small businesses.

25 The other thing that's really a benefit to

1 small businesses is the defined timeframe in which
2 coordinated review occurs. So when you file with the
3 state, the lead state is Washington State, within 21 days
4 you receive a comment letter from the states that are --
5 that you have made your filing in.

6 The first state, the first issuer, the issuer
7 under the Regulation A coordinated review process was a
8 company named Ground Floor. They registered in ten
9 different states. They got their comment letter in ten
10 days. They responded to the comment letter and as you
11 see in the coordinated review the states got back to them
12 within five days after that.

13 So they really appreciated the defined
14 timeframe in which they could operate. Nick Bhargava,
15 who is one of the co-founders of Ground Floor, I spoke
16 with him yesterday in preparation and he said that the
17 defined service standard really allowed them to manage
18 their cash flow more efficiently, save them money. They
19 knew when they were going to have legal fees, they knew
20 when they were not going to have legal fees for certain
21 months. So he really appreciated that. And the process
22 for them took about six -- or sorry, took about three
23 months to clear. They were cleared through the states
24 and they're still waiting on comments from the SEC to
25 reach -- to get cleared at the federal level and go live

1 with their offering.

2 So that's sort of the overview of coordinated
3 review. We're as I mentioned very excited about it. We
4 have two other filers that are in the comment process.
5 We think that it's going to be a successful program.
6 It's something that can be adapted to Regulation A+
7 offerings and we think it makes sense because oftentimes
8 these offerings are more of a local nature. Nick also
9 mentioned that state regulators, being that the offerings
10 are more local, were more accessible to him, that he was
11 able to get on the phone, send e-mails to the lead
12 examiners that were providing him comments and they could
13 all sort of have a big pow-wow and talk through the
14 comments and not have to go through a formalistic comment
15 letter process, which really, you know, allowed him to
16 save time and money in terms of responding to state
17 comments.

18 The other major thing I'll mention about
19 coordinated review is that the task force that put this
20 together worked with the ABA Small Business Law Group and
21 said which are the substantive standards that business
22 have the most difficult time complying with when it comes
23 to Blue Sky Law. And NASAA internalized that and in the
24 coordinated review process has relaxed the so-called
25 statements of policy standards that apply to small

1 businesses, again making it easier for small businesses
2 to get approved under the state system.

3 MR. REESE: Thank you, Mike. I have a
4 question.

5 MR. PIECIAK: Yes.

6 MR. REESE: Is this review, this coordinated
7 review program available for all states?

8 MR. PIECIAK: So 46 states have signed up to
9 date. New York is a notice filing state. So
10 qualification in New York is unnecessary. We just spoke
11 with some folks in Arizona recently. That's one of the
12 states that's outstanding. We're hoping to get them on
13 board. Georgia is another state that's outstanding. I
14 just spoke with the Georgia staff. Every single person
15 in the Georgia staff is new as of six months ago I think.
16 They had a large overhaul. So they're working up this
17 process of getting it approved in Georgia. And then the
18 last state is Florida, which is also going through a
19 rulemaking process. So it's just taking them a little
20 bit longer to get approval from their home state.

21 MR. REESE: Okay. And then finally on the
22 exchange, the payment exchange, is that a single pay or
23 electronic exchange? Can you tell us how that works?

24 MR. PIECIAK: Yes, sure. That's another thing
25 that we're excited about. It's called the electronic

1 filing deposit, EFD. It's not ready for Regulation A or
2 Regulation A now. We just made it available for 506
3 offerings so that you can seamlessly file all of your
4 payments with all of the states electronically.

5 I should mention that a coordinated review
6 otherwise is electronic. You can submit your documents
7 electronically to Washington and they disburse them to
8 the particular states. But we're working toward getting
9 EFD to be the system that you file through when doing
10 Regulation A offerings. So that process would be
11 streamlined.

12 Yes?

13 MR. GRAHAM: Any other questions? Oh, Sarah?

14 MS. HANKS: I've got a question. So the first
15 filer through the system do I understand it's been three
16 months and they're still not finished?

17 MR. PIECIAK: I'm sorry. So they filed on
18 August 20th of 2014 and they received final clearance
19 from us on January 30, 2015. So they're cleared from the
20 states, so they're still waiting for comments from the
21 SEC.

22 MS. HANKS: Okay, thanks.

23 MR. PIECIAK: Yes.

24 MR. GRAHAM: Other -- yes, John.

25 MR. BORER: Along those lines, if you could

1 give an idea or explain if you know how these
2 requirements, this system, would interface with the
3 Division of Corporate Finance and their review process
4 with respect to Reg A and Reg A+ filings to streamline
5 the process and perhaps to avoid inconsistencies if each
6 of the groups are coming down different paths at
7 different times.

8 MR. PIECIAK: Yes, sure. Well, I mean, right
9 now the answer is that they don't interface. I think
10 it's an excellent point. I think it's something that the
11 SEC and NASAA can cooperate on to figure out how we can
12 streamline the process better.

13 One example from Grand Floor that I can mention
14 is that there was a comment letter that they received
15 recently that was an issue that had already been resolved
16 at the state level, and they had some frustration with
17 the fact that they have to deal with that issue now sort
18 of six months in their review process. So if the states
19 and the SEC were able to work better then I think that
20 would be something that would benefit small business
21 issuers certainly.

22 MR. BORER: As a quick follow up to that, if
23 there were inconsistencies between the interpretation or
24 evaluation of issues of disclosure in the Reg A or Reg A+
25 once fully adopted how would you propose that those be

1 reconciled in a practical fashion for an issuer to do
2 that if there is no coordination formally built into the
3 system?

4 MR. PIECIAK: You mean a substantive comment or
5 some structural --

6 MR. BORER: Yes, different accounting
7 treatment, different interpretation of the risks of the
8 business, et cetera.

9 MR. PIECIAK: Well, I mean, those are the type
10 of -- I mean, that system is -- the system between the
11 SEC the states has been in place for about 100 years or
12 so. So I think business and the SEC have been able to
13 treat those comments and discrepancies adequately for a
14 long time. So I don't know if that's really necessarily
15 a prevalent issue. But certainly in addressing comments
16 for either states or to the SEC issuers are allowed to
17 fill us in on what other regulators have told them, what
18 comments are from other regulators, and we'll take that
19 into consideration when considering our comments.

20 So I think it is -- even though it's not a
21 formal collaborative process, I do think it's more
22 collaborative than maybe it's led on to believe.

23 MR. GRAHAM: Charles.

24 MR. BALTIC: Thank you, Mike. Would the 46 or
25 so participating states retain the ability to withdraw or

1 amend their participation in the coordinated review
2 process?

3 MR. PIECIAK: Well, states certainly can do
4 what they're going to do, but all states have agreed to a
5 memorandum of understanding that they will participate in
6 this program, and most important of which is that when
7 that lead examiner is chosen for an offering that when
8 the lead examiner decides an offering is cleared that all
9 of the other states agree that it is cleared in their
10 state as well.

11 So there is that sort of structure in place
12 that mandates that states that have agreed voluntarily to
13 participate in this to have the offering cleared in their
14 state. And just as a practical matter, I mean states are
15 aware and states really appreciate the fact that this
16 coordinated review process was a big step forward, but it
17 was also a necessary step forward and in the state's own
18 interests they have to cooperate and move forward
19 together. So it's really to the state's advantage to
20 participate in this and to move forward.

21 MR. GRAHAM: Greg.

22 MR. YADLEY: Thank you, Mike. It certainly is
23 a step forward. I wanted to ask you a little more about
24 the local character really in two regards. With larger
25 offerings up to \$50 million why do you think that the

1 filers using Reg A+ would necessarily be local in
2 character? And then second if you were appointing a lead
3 examiner from among the 46 states wouldn't that examiner
4 many times not be local with respect to the particular
5 offering?

6 MR. PIECIAK: Yes, I think that's a good point
7 on both questions. I'll address the second one first.

8 I mean, who is the lead examiner obviously
9 depends on workload and things like that. But also
10 there's a flexible process, so if there is an offering
11 that's in Georgia and Georgia is participating the lead
12 examiner could be Georgia. I think oftentimes you see
13 state regulators in other coordinated contexts put a
14 regulator that's local. I think that just makes sense.

15 Regarding the \$50 million threshold, I guess
16 there's sort of two points to that. One is that not all
17 offerings obviously will be \$50 million. There will be
18 smaller offerings than that that are local in character.

19 Even offerings, though, that are at \$50 million are
20 rather small in today's economy. I mean, they're much
21 larger than \$5 million. But you could easily see -- you
22 know, I could easily imagine an offering of \$50 million
23 that registers in only a handful of states for strategic
24 reasons for their business plan. For example Ground
25 Floor is a real estate loan company. They registered in

1 the states that they thought had the highest percentage
2 of real estate volume. So I think you'll see offerings
3 that remain local in character either that take advantage
4 of the \$50 million or that don't.

5 MR. GRAHAM: Okay. Yes, Sonia.

6 MS. LUNA: Michael, can you walk us through the
7 process of assigning a lead examiner on these deals?

8 MR. PIECIAK: Sure. So the administrative
9 state is Washington State and they receive all the
10 paperwork. They send out the paperwork to the other
11 states and they decide in collaboration with the states
12 that are in the issue who is going to be the lead
13 examiner. And it's really an informal, collaborative
14 process. There's not as far as I know a formal structure
15 in place.

16 Does that answer your question?

17 MR. GRAHAM: Okay. Should we move to DJ?

18 MR. PAUL: Sure. I mean, I guess I'm going to
19 start a little bit more in than I had intended, which is
20 totally fine because other members of the committee have
21 already asked the smarter questions than I would have
22 come up with.

23 I would just go back and just do a little bit
24 of history here. Reg A is not something from the 80's
25 and the 90's. It existed pretty much as old as this

1 agency. It goes back to '34. And in that time it's been
2 -- you know, sometimes you do things and they don't
3 always work. This is one of the things that has never
4 really worked correctly.

5 The numbers that Michael referred to are
6 accurate. I would just say that in terms of qualified,
7 the peak being in '97 and '98, there were 57. That was
8 at the peak of qualified offerings, which dropped to one
9 offering in 2011.

10 So clearly this is not something that the
11 market has adopted. And while the four reasons given
12 just from the GAO study as well as just talking to
13 practitioners, yes it's true that Reg D has made it less
14 necessary perhaps and the \$5 million cap is a
15 contributing factor. Talk to a practitioner, talk to an
16 attorney, talk to anyone that's in the space and they're
17 going to tell you that it's the state -- it's the state
18 requirements and the Blue Sky requirements that are the
19 single biggest obstacle both in terms of cost and just
20 being unctuous.

21 While I certainly appreciate NASAA attempting
22 to come up with yet again, and I'll get back to that in a
23 second, a coordinated review program, I would note that
24 this is more evolutionary than revolutionary and that
25 they've been trying to come up with something since the

1 80's and every previous attempt has pretty much failed.
2 I could go into the details of the previous iterations of
3 the state -- coordinated state review process from, you
4 know, the regional scores to the -- I can't remember what
5 the -- how one pronounces this but the MIIE program. And
6 it's never been 50 states, it's never been all
7 jurisdictions, and it still isn't.

8 And the problem is that now we are into the --
9 we have several problems. First there's this thing
10 called the interwebs, and state boundaries don't match
11 much when you're doing offerings. So it's really sort of
12 an all or none. It's either federal or it's not. Its
13 either the entire, all jurisdictions, or it's not. And
14 it can't be awfully close. It has to be right or you're
15 going to leave yourself subject to some sort of
16 enforcement action.

17 I think Charles's question, I think it was
18 Charles, as to whether or not a state could at some point
19 opt out is an apt one because NASAA doesn't have
20 enforcement ability with respect to its members. And if
21 we as group and the SEC as a body were to adopt this as,
22 which is to say the multi-state coordinated program as
23 proposed as some sort of ersatz state preemption, in
24 short order, or maybe not so short order but at some
25 point in the future it could become more problematic if

1 states either in masse or just five or six more
2 significant one were to opt out and then we're back to
3 where we started again.

4 I like Michael and I want to be as deferential
5 as I can to him and his organization, but I don't believe
6 that a proof of concept of one company that took the
7 better part of six months, that seems specious to rely on
8 that when there is a great deal of precedent for NASAA
9 attempting to do this and failing to do this. Goodness,
10 they've had 80 years to come up with this and now at the
11 eleventh hour as we are contemplating this there is a
12 nifty new program that's supposed to be great and the one
13 company, one company that's gone through was approve
14 something like, I don't know, five weeks, less than five
15 weeks ago.

16 So I have some reservations with respect to the
17 efficacy of this program and whether or not it really
18 would be something that would work.

19 I would also point to the fact that I have
20 heard the arguments of course with respect to whether or
21 not the SEC is overstepping its bounds in the
22 congressional intent. I would not want to litigate that
23 or even attempt to adjudicate that, but I would simply
24 say that for those of us who were involved at the time --
25 first of all, divining congressional intent is always an

1 interesting process and I'll leave that one there.
2 But nevertheless for those of us who were involved
3 at the time there was no consensus -- there was less of a
4 consensus on this issue. It wasn't that it was suggested
5 that state preemption should not be part of this, but
6 rather that it should be left to the experts. One could
7 call it a punt if one wanted to use such language, but
8 the idea was that the SEC should make that determination.

9 That doesn't suggest that the SEC is overstepping its
10 bounds with respect to contemplating some sort of state
11 preemption, rather it suggests that the SEC was empowered
12 by the Congress to make this very determination that we
13 are discussing right now.

14 I don't think that there's any question for
15 those us who like work in the universe of trying to help
16 small companies form capital that state preemption is
17 crucial to a successful Reg A. It will continue to be a
18 dead letter as sadly it has been for the better part of
19 80 years or maybe it's a little more now if that doesn't
20 exist. It's really about that simple. I don't -- I
21 think that NASAA's attempt to come up with a coordinated
22 review speaks to that. I think they realize that, and so
23 they're trying to come up with something. I don't trust
24 that this works. I don't think that it's a good
25 substitute for it even if it were to work and I don't

1 think it's binding. So I don't think it's something that
2 can be relied upon and that lack of uncertainty in itself
3 is problematic.

4 I've got more to say on it but I feel like I've
5 taken up enough time. But that's more or less my position
6 with respect to this. I think without state preemption
7 we should contemplate moving on to other forms of capital
8 formation for small businesses.

9 MR. GRAHAM: Thank you. Questions? Comments?
10 Charles.

11 MR. BALTIC: Yes, I wanted to follow up on DJ's
12 comments. You know, in my experience uncertainty is
13 really very antithetical to capital formation and
14 investment. You know, while it's laudable the efforts to
15 make this a program which would facilitate this review,
16 streamline it, make it uniform, you know, there are
17 several elements that seem to be uncertain -- not all
18 states participating, states retaining the option to
19 amend or opt out of participation, no formal or
20 formalized structure to choose lead examiners and limited
21 visibility into the interface with the Commission's
22 Division of Corporate Finance.

23 So I understand it's a new proposal, but I
24 think we hear in the remarks from the Commissioners that
25 there is some emphasis and urgency with respect to trying

1 to make these revisions and get Reg A+ to be a viable
2 method and a utilized method for fundraising. And I
3 think requiring small issuers to comply with divergent
4 securities laws in an uncertain and untested forum would
5 likely discourage utilization of Reg A offerings, which
6 is the goal.

7 So I do have concerns about this and I think
8 the broadest possible definition of qualified purchaser
9 to facilitate Reg A+ and its utilization I think is
10 appropriate.

11 MR. GRAHAM: Thank you. Greg.

12 MR. YADLEY: And again, Michael, I think this
13 is a really nifty idea, but I think it almost begs the
14 question of what really is to be gained by it. The
15 interesting thing about capital formation for the last
16 ten years has been this blurring of the line between
17 public and private offerings, and at some point I think
18 we sort of need to step back and look at it all as a
19 piece. But it's starting to come together and if you get
20 far enough away from the individual pieces it is working.

21 Reg A as you said is really an exemption and it
22 has been. I've done Reg A. The last time I did one was
23 1984, so it's been a really long time. It was an oil and
24 gas company in Florida. And I practice in Florida now
25 and I'm mindful of how difficult my state can be in terms

1 of getting on board with all the other states.

2 But Reg D and in particular Rule 506 without
3 much regulation has worked well as a capital formation
4 tool, and as this committee has discussed and the
5 Commission staff is aware I believe the fraud in
6 connection with those activities is really not related to
7 the fact that it's an exemption. So in a way I think
8 that with the increased dollar limits on Regulation A+ we
9 should look at this as in fact a more regulated type of
10 offering than Rule 506 and we should give it a Chace.
11 And I certainly believe that smart, experienced,
12 state securities regulators can have more comments which
13 would be beneficial to the issuer, but I really don't
14 know incrementally how much that addresses. I think that
15 the SEC should move ahead with its proposals and there
16 should be preemption, and I think the states will have
17 full authority in the enforcement area.

18 But my overall comment would be that I am
19 pleased because there are other areas that will also lead
20 to capital formation initiatives, including private
21 placement brokers and others where I think it's very
22 important that NASAA take the lead in rounding up the
23 states and trying to have them work together. But in
24 this area I think SEC review will be sufficient for
25 investor protection.

1 MR. GRAHAM: Thank you. Mike.

2 MR. PIECIAK: Thanks, Greg. I just wanted to
3 mention one thing that we hadn't talked about which
4 speaks to Greg's point about review, and it's more of a
5 practical point that if Regulation A+, the market does
6 take off as we hope it does and there are a number of
7 issuers that are successful, whether or not -- and the
8 states are removed from the process, whether or not the
9 SEC has the staff to review the offerings in a timely and
10 efficient manner like they do now would be I think a
11 serious question.

12 And I think the result is either that offerings
13 are delayed or offerings don't get the type of review
14 that they do now, and both of which I think are bad for
15 capital markets if there is some retail investors that
16 get burned in the Regulation A marketplace. At the onset
17 I think we run the risk of the Regulation A marketplace
18 looking like something that legitimate businesses do not
19 use, and that's obviously not what any of us want to have
20 happen, so in leveraging state resources and being able
21 to get examiners to look, get eyes on offerings, not
22 necessarily just to weed out fraudulent individuals but
23 to make the offerings more better, to make the -- to give
24 substantive comments that make the offerings better for
25 the issuers and for the marketplace.

1 So that's the only point that I'll make there.

2 MR. GRAHAM: John.

3 MR. BORER: I'll give some opinion here. First
4 of all I think the SEC running out of staff to review
5 these things is probably not the reason to put somebody
6 else other than the SEC on the case. In my view what the
7 coordination angst with the states is, and I'm saying
8 this as a practitioner on Wall Street for many, many
9 years, is just subjecting the same offering to a
10 second flogging, and putting that in the pejorative to
11 some degree and a very redundant set of circumstances.

12 And I believe, and the point that was made a
13 couple of minutes ago, the potential differences and
14 disparity substantively in the qualifications of the
15 various state securities commissioners may have an impact
16 on the quality and the timing of the review.

17 And it sounds to me that while there is some
18 Coordination, it's sort of a lottery wheel being spun as
19 to who is going to be reviewing it, how substantive that
20 review may be based on the qualifications of the office
21 that's doing the review. Where at least with the
22 Division of Corporate Finance there appears to be as I've
23 experienced over the years a very consistent application
24 of standards to the review process. And I think taking
25 and making things less certain goes against the intent of

1 the legislation.

2 MR. GRAHAM: Thanks, John. Mike.

3 MR. PIECIAK: Very, very brief point because I
4 don't think I was very clear at the onset. The lead
5 examiner acts as a coordinator between the issuer and the
6 other states. So the fact of who the lead examiner is is
7 less of an issue as to what states you're filing through.
8 All the states will review the offerings, give their
9 comments to the lead examiner, who will then work with
10 the state regulators to iron out any conflicts or
11 discrepancies and then send those and any duplicative
12 comments, and then send those comments to the issuer.
13 So there is a fulsome review and the lead examiner
14 is less important as to the substantive review of an
15 offering as to the sort of procedural interaction with
16 the issuer if that makes sense.

17 MR. GRAHAM: Okay. Anyone else? We haven't
18 heard from everyone. This is -- do you want me to call
19 on people?

20 MR. REESE: You've heard from me, but I am
21 sitting here and I am asking myself some questions that
22 maybe I'll express outward and ask a few more questions
23 than Mike. Because I think the conversation originally I
24 thought was between Mike and DJ presenting information
25 about their idea of the Reg A market to give us

1 background, where I think we're responding to Mike's
2 discussion around a coordinated review program. But I
3 don't think we're trying to adopt that. That's my first
4 impression is I'm not trying to sit here today and say
5 this is what we're going to adopt.

6 But I do think it's interesting that they are
7 looking at this and I wanted to know more about some of
8 the -- how this program works. In my mind I hear you
9 talking about the State of Washington and its securities
10 director to be more of the clearinghouse if you will.
11 And how did -- how do these things come about? I really
12 want to understand how this -- how did this come about.

13 Because my concern is this going to be in
14 competition to or how is this going to be viewed in the
15 marketplace. So before I get to that part I just want to
16 understand more about the clearinghouse aspect, the idea
17 that they are the centralized person operating with the
18 issuer and how do they handle caseload and workload and
19 how does all that happen as well. And what are the
20 numbers you expect? Have you done any volume sort of --
21 how does this scale? Okay.

22 MR. PIECIAK: The practical reason for having
23 Washington State be the coordinating sort of state was
24 that they have a strong history of corporate finance, and
25 have a strong corporate finance team, and have sort of a

1 deep bench. So that made sense to the states. They had
2 the willingness to take this on, and Faith Anderson who
3 is a very important part of their office really
4 shepherded, coordinated the review through all of the
5 states and put it on her back and got it to where it is
6 today.

7 So it was really due to their expertise and
8 their manpower. Whether -- the extent to which this is
9 scalable, right now there are two other offerings in the
10 system. We had a third, a third that got approved. It
11 was approved in about four months.

12 State regulators have a lot of staff. I mean,
13 I think we could handle quite a few offerings. The fact
14 that the lead examiner sort of rotates depending on the
15 workload of that state provides the state some
16 flexibility in terms of responding to a number of
17 offerings, whether they're all at the same time or a
18 number of them are under review at the same time.

19 But in terms of actual numbers I can't give you
20 an actual number other than to say there's quite a large
21 number of resources among the states.

22 MR. GRAHAM: Thank you. Dan.

23 MR. CHACE: Can I ask a question because this
24 is way outside my area of expertise. But I do read the
25 comment letters from the SEC of publicly filed companies

1 and they always reflect a thorough and really interesting
2 perspective on the filings that the company has made.

3 Is it fair to assume that for this type of
4 filing that we're talking about, Reg A, that the SEC
5 review would be as thorough as it would be for a public
6 company?

7 MR. HIGGINS: I mean, that's probably addressed
8 to us and the answer is that we treat -- in the Division
9 of Corporation Finance they're reviewed by the same
10 people that review S-1s, S-3s, you know, et cetera, and
11 the kind of review we give it. I mean, we recognize that
12 the exemption is somewhat different than our S-1 system,
13 but within that context we give it the kind of review
14 that we would give any filing that we give a
15 qualification to.

16 MR. CHACE: Just, okay, because my point then
17 was that those reviews reflect a very thorough review in
18 my opinion that is sufficient. I mean, it reflects good
19 work.

20 MR. GRAHAM: Thanks, Dan.

21 MR. GALLAGHER: Can I ask a question, Steve?

22 MR. GRAHAM: Please, yes.

23 MR. GALLAGHER: Because it's an all too perfect
24 segue for something I wanted to touch on, which we're
25 talking a lot about process as if its competition or an

1 analysis of the mechanisms by which the SEC would do the
2 review versus NASAA. So in doing so, and I think Mike
3 makes some good points about how they've done these
4 refinements, I think we're skirting around the real issue
5 to me which is merit regulation versus not merit
6 regulation.

7 And I think that's what Dan hits on.
8 Our staff reviews the filings to see if they're in
9 accord with our rules, but it's really a disclosure
10 model, right. It's not merit. And I think underlying
11 some of the concerns on process, and no one has come
12 right out and said it so I'll do it for you, is the
13 notion that we'll go back in time and one of your states
14 may decide that the latest tech company is not worthy of
15 its residents and they either pull out of the MOU or may
16 convince the others that we should just proscribe it
17 instead of going through our process and making sure the
18 disclosure is there.

19 And that to me is a concern because it's not
20 hypothetical. We got to Massachusetts and think about
21 Apple and that worked out well. So that's what I worry
22 about when I think about our mission on capital
23 formation. It's the capital that never happens, right.
24 It's not the disclosures, or the process, or the expense,
25 or the delay. I mean, there's -- you know, entrepreneurs

1 are willing to put up with a heck of a lot. I've learned
2 that in my tenure as a commissioner. They are, you know,
3 a tough crowd. But if there's the potential for sort of
4 nanny-stateism, the merit review, the we just don't think
5 this is good for you, I think that's why you hear folks
6 wanting to come to us. We just don't and can't and
7 shouldn't do that, right. If you don't meet the legal
8 requirements we're not going to allow you to go forward
9 with your offering. But that's the measure and there is
10 caveat emptor built into our system.

11 So I'm just curious from the committee to what
12 degree that plays into outside the process because I
13 think we're buried in the process right now.

14 MR. GRAHAM: John.

15 MR. HEMPILL: One thing that I wanted to
16 mention, and first of all I haven't done anything with
17 Blue Sky since 1985 so I'm appreciative of that. But
18 before then I did a lot of work. I used to do registered
19 junk bond offerings for Drexel Burnham back in the day
20 and we would do 50 state registrations.

21 One of the things that's kind of disturbing about
22 this is that oftentimes we would hit a state, usually it
23 was either Texas or Massachusetts, we always go through
24 California because we had a local counsel there, but
25 sometimes you just hit a roadblock with a state and you

1 just say forget it. We're not going to sell in
2 Massachusetts or we're not going to sell in Florida.

3 This process seems to basically say it's kind
4 of an all or nothing process. And is there any way that
5 -- you know, it's like if there's one state that really
6 doesn't like the offering and is giving a bunch of
7 comments is there any way to kind of say, fine, we won't
8 go in that state well go in the other 45 states?

9 MR. PIECIAK: Yes, that's a good point. The
10 issuer is free to withdraw from a state along the process
11 and have the other states continue with their review or
12 have a follow on where they add additional states as the
13 process moves forward.

14 MR. HEMPILL: And is there a way to identify
15 which comments come from which state?

16 MR. PIECIAK: Yes. There are state specific
17 comments at the end of a comment letter. There's a
18 general -- they're general comments that sort of apply to
19 all states, forms and what not, and then the specific
20 state comments are in the back of the letter.

21 MR. GALLAGHER: Mike, before I -- on the flip
22 side, sorry, if a state -- can they pull out too? I
23 guess it's the same right? So the issuer can pull out of
24 a state but one of the states can say we just can't sign
25 on to this letter and pull out and therefore you wouldn't

1 be okay in that state?

2 MR. PIECIAK: Well, I think the state, in
3 practical terms a state would have its comments that they
4 want addressed and the issuer would be unwilling to
5 address them. So then it would up to the issuer to say
6 we're withdrawing our application in the state.

7 MR. GALLAGHER: Got you. Got you.

8 MR. GRAHAM: Okay. Sonia?

9 MS. LUNA: So this kind of question is more for
10 DJ. I wanted to kind of summarize some of the solutions
11 that I think you were offering, which is all or nothing.
12 Was your recommendation that the SEC have a ruling or
13 something in place where all 50 states have to abide by
14 it or -- I wanted to make sure --

15 MR. PAUL: No, my recommendation is that the
16 states shouldn't be conspired with respect to Regulation
17 A, that there's precedent for state preemption in various
18 different guises from, you know, part of Reg D and the
19 pending Title 3. It's my suggestion and -- or it's my
20 opinion that Congress not only gave the SEC authority to
21 decide this issue but gave the SEC -- has burdened the
22 SEC with the obligation to decide the issue and that the
23 recommendation of this committee should be to have the
24 SEC light up the proposed Regulation A+ regulations as
25 they have been proposed and with all deliberate speed.

1 And I no longer want to consider the state issue at all.
2 That's my recommendation.

3 MR. GRAHAM: Okay. Sara.

4 MS. HANKS: I just wanted to make the very
5 simple mathematical analysis that it is twice as much
6 work to go through two registration processes as it is go
7 through one. And however good the coordinated review
8 system is it is still going to be a whole other thing. I
9 just wanted to bring it back to the point of view of the
10 companies, and we're talking about very small companies,
11 companies who are cash constrained, companies who are
12 under the gun.

13 I'm working with a really cool clean tech
14 company who went through the SEC review process for Reg A
15 towards the end of last year, started with an offering
16 statement that got approved through the statement --
17 through the review process, went to one of the states,
18 got the first set of comments back and said we give up.
19 We can't do it.

20 So they took what would have been a Reg A, much
21 more transparent process, and they're going Reg D right
22 now and it's much faster.

23 So looking at it from the point of view of a
24 company it is just -- it's taking twice as long and it's
25 just a very, very simple fact and this really matters for

1 small companies.

2 MR. PAUL: Just as I pointed out, it's just not
3 time it's also money, right. The fees still need to be
4 paid even if you coordinate the review. So, you know,
5 for smaller offerings, yes, it's nice that we're going up
6 to \$50 million, and then I guess if you were even close
7 to that this becomes less relevant. But if you are in
8 the habit, the sweet spot or whatever, the vast majority
9 of Reg D offerings being the closest analog, which isn't
10 just below \$5 million, I believe it's below \$3 million,
11 just in terms of the average raise size, the additional
12 cost here will make it prohibitive and it will simply be
13 as it has been, it will be Reg D. So it's not -- time is
14 of course a factor and it always is. Efficiency is a
15 factor. Money oddly is also a factor.

16 MR. GRAHAM: Okay, all right. Greg?

17 MR. YADLEY: Just a footnote. I don't share
18 DJ's cynicism but I did have in mind Commissioner
19 Gallagher's comment about the fair, just and equitable
20 standard. I didn't bring it up because I don't think we
21 quite have to get there but it does inform what we're
22 talking about. NASAA is an organization and its done
23 wonders in coordinating 50 sovereign jurisdictions, but
24 that's the problem.

25 If we're going to have state review and the

1 states are going to take their responsibility seriously,
2 state representatives have to say what they think. And
3 you can't really coordinate all that, and even if you
4 could to have to then take the time and the money to say,
5 okay, well we're almost done but we have these three
6 states that we may not be able to sell in, you know,
7 that's several thousand dollars of lawyer time right
8 there thinking about how that's all going to work out.

9 And again back to something I said earlier, the
10 comments will be useful and in many cases they would
11 improve the offering, but \$50 million we all agree that
12 probably the average won't be \$50 million. For the
13 smaller offerings how much more refinement and benefit
14 does an investor get by yet another person's view? I
15 mean, within the building here different staff members
16 have different views of offerings. But there's a
17 hierarchy and at the end of the day Keith is chair of the
18 division and if he has to get involved, which is very,
19 very minimally because we have the associate directors
20 and the assistant directors and the branch chiefs, but it
21 can get done and it gets done within the 30 days.

22 And again I feel like I'm pouring cold water on
23 what's been a marvelous effort of the states to work
24 together, but I just don't think in this context where
25 we're trying to experiment small amounts of capital being

1 raised by non-reporting companies that we should do it at
2 the outset. If it doesn't work we can always revisit it.

3 So I support DJ's viewpoint with a slightly more civil
4 tone.

5 MR. GRAHAM: Okay, let's just go around and
6 then let everyone sign off starting with you, Tim.

7 MR. REESE: Okay. Well, I wanted to respond to
8 Commissioner Gallagher's question about capital doesn't
9 get formed, not the capital that's already being formed
10 in the market and the concern. And what I think about is
11 over my 21 years as the idea of what the current Reg D
12 offers and how that money gets accumulated into a deal,
13 and why I think it was chosen from the 90's, 2000, is,
14 one, because it became the boilerplate of convenience.
15 It's one of those ones where everyone kind of learned how
16 it operates.

17 And the way you form capital for these
18 unregistered securities is the issuer knows through a
19 lawyer, and in some cases even in house, the ability to
20 put together a PPM, right, that says these have not been
21 registered. And they understand about how to -- and
22 lawyers' fees have drastically dropped around this area
23 because there's so much going on in that market, about
24 how to put that deal together. And then it becomes
25 incumbent upon him or her when they go to, primarily to

1 the Angel marketplace and then present.

2 And then the due diligence, the onus of the
3 research becomes that of the Angel investor through a
4 lead. And that's how we've been doing it throughout for
5 myself for over a decade plus.

6 And it gets into something that Commissioner
7 Aguilar wanted to talk about, the piggyback and the fact
8 that the due diligence process is such a costly, time
9 constraining process, and about the time that issuer hits
10 you, I need \$2 million or I'm out of business, you know,
11 this -- you hear all this and it becomes a little bit of
12 are you going to respond that fast or if you are really
13 so moved by that opportunity.

14 So I think what happens is there's a cost
15 structure, there's a cost impediment right now that we
16 need to kind of simplify the ability to create a venture
17 exchange where smaller companies, those that I work with
18 and others that I think about who have exciting -- they
19 have exciting business potential. They're bringing
20 strategic investors but they're not quite big enough to
21 get into institutional size, and going the route of an
22 Angel quite actually is a little bit cumbersome because
23 that could take you 18 months to two years.

24 And so we have to be able to solve a way that
25 would be a way that would allow their deal to kind of get

1 out there in front of potential investors and they have
2 the confidence that that deal has been vetted and the
3 comments have been appropriate so that they can make an
4 informed decision. So that's my opinion around that
5 area.

6 MR. GRAHAM: Do you have anything more to add,
7 DJ?

8 MR. PAUL: Sure, but I'm not going to.

9 MR. GRAHAM: Okay, fair enough. You've --
10 okay, DJ gives his time to Catherine.

11 MS. MOTT: I'm going to make it simple. I just
12 agree with Greg's comments and his summary of DJ's point
13 of view. So I agree.

14 MR. GRAHAM: Anything to add, Sonia?

15 MS. LUNA: I agree with DJ's comments earlier.

16 MR. GRAHAM: John.

17 MR. HEMPILL: Me too.

18 MR. GRAHAM: Sarah.

19 MS. HANKS: Well, I also agree with DJ but have
20 something to add, which is there is compelling public
21 policy reason to make Reg A workable because it is
22 transparent, it adds to the information that's available,
23 it adds investor protection, and the only way you do that
24 is -- I'm sorry, preempting state regulation.

25 MR. GRAHAM: Milton.

1 MR. CHANG: I think on paper it sounds,
2 theoretically it sounds very good, but I think as a
3 practical matter I'm not sure it's going to be that
4 efficient.

5 MR. GRAHAM: Okay. Dan.

6 MR. CHACE: Nothing to add.

7 MR. BORER: Well, I'm a big believer in state's
8 rights, but I think in this case if we want Reg A and Reg
9 A+ to become effective then we're going to need
10 preemption.

11 MR. GRAHAM: So what, are we going to have a
12 state's rights debate now? David.

13 MR. BOCHNOWSKI: I'm on the side of preemption.
14 It's just a little bit beyond my confidence, filling in a
15 public company once, gone through the process in 1984.
16 But I have 35 years of experience of dealing with
17 amateurs on the banking side. And the challenge is that
18 we all have our proclivities and our biases and our
19 belief in what's right.

20 One time during an examination and the lead
21 examiner asked me why we're doing it a certain way and
22 the best answer I had was because the guy before said we
23 should do it that way.

24 And that gets back to the biases. I think that
25 the congressional intent all along has been for federal

1 preemption. I know that in the banking business it
2 works very well, and perhaps the need that the states are
3 seeing is one that is real, but perhaps if the SEC can
4 become more nimble it will resolve itself. And so I
5 favor preemption.

6 MR. GRAHAM: Thanks, David. Charles.

7 MR. BALTIC: I agree with DJ and John and
8 others that in this setting, in this particular setting,
9 really a national standard would be very important to
10 reinvigorating Regulation A as an important tool for
11 capital formation. Thank you.

12 MR. GRAHAM: Anything Chris? Do you want to --

13 MS. JACOBS: Yeah. I guess I would weigh in --
14 I'm going to agree with the, with the consensus in the
15 committee. But one thing, you know we've been talking for
16 almost an hour. We never talked about what additional
17 protections this two tier system is bringing to
18 investors.

19 And so I kind of was netting this out like
20 what's a secondary or a primary tier of regulation. What
21 additional protections is that bringing the investors? I
22 didn't hear that this morning.

23 So I'm -- I don't -- in fact I kind of heard we
24 were discussing not investor protection but maybe turf
25 issues, and having been a sitting CEO of a public company

1 I have to say I thought to the points made here that the
2 questions, the comments, and the regulations of the SEC
3 they're well in place. We all understood them. I know -
4 - if you're going to have a costly review understand your
5 turf and understand there's precedence out there, which
6 is I have found where the SEC rules were concerned did
7 indeed -- there was precedence and as an issue whether
8 you understood the game, and how it was going to be
9 played, and what you had to do to comply.

10 And I go back to what our goal is as a
11 committee, which is to foster capital formation, and in
12 this case I think the additional cost and taking these
13 folks off task is not -- I can't go with it. So I'm with
14 the rest of the room.

15 MR. GRAHAM: Thanks. Well, thank you, DJ and
16 thank you Mike for teeing that up for us, and thank you
17 all for your thoughtful comments.

18 MR. GALLAGHER: Stephen, can I make one last
19 point before you -- this is me, to your right.

20 I wanted to close out my own thought. And
21 first it wasn't fair I didn't think to thank Mike for
22 being here and doing such a great job with the
23 presentation, because I now understand the process
24 better. And I think it's going to be an important
25 process one way or the other, whether it applies to a

1 certain portion of Reg A, all of Reg A or not. So I
2 really do think that's critically important.

3 And I didn't want to leave one thing Sarah just
4 said, and why this is important, why Reg A is important.

5 You know, we have to remember when we're talking about
6 comparisons with Reg D and other exemptions these are not
7 the millionaire markets. These are quasi-public
8 offerings, right. And one of the things we don't do here
9 enough is ensure that there's democracy in capital
10 raising and that everyone can participate.

11 Now I understand that brings with it attendant
12 risks potentially to less sophisticated investors, and
13 the states will always have a role to play there as well
14 the SEC. So we do have to worry about Chris's concerns on
15 investor protection. I think that does go to the debate
16 between merit regulation versus disclosure based
17 materiality regulation. I think they both serve investor
18 protection in their own way. But we can't lose sight of
19 the fact, and that's why we're talking about venture
20 exchanges with such vigor in the context of Reg A, that
21 these are the every man and every woman markets, not just
22 the millionaire markets. And I think that's a critically
23 important distinction to keep in mind as we go forward.

24 So sorry to interrupt one more time --

25 MR. GRAHAM: No, no. Thank you.

1 MR. GALLAGHER: -- but this is something that
2 motivates me as I think about these issues and I want to
3 share it with you guys.

4 MR. GRAHAM: No, not at all. Thanks.

5 I think everyone has said it well. I don't --
6 I don't need to repeat those comments. I think that
7 preemption in this context makes a lot of sense and it
8 sounds like there is a consensus on the part of the
9 committee to go in that direction. I think what I would
10 like to do is to issue a recommendation broadly on the
11 basis of DJ's comments, and with the idea being that this
12 time we won't have to take a little more time in fine
13 tuning the actual recommendation and getting it out to
14 people so we can work on it.

15 But it seems to me that there's a clear
16 consensus in this context that the state preemption is
17 something that would take friction out of the system and
18 would help to achieve the goals that we're trying to
19 achieve in terms of facilitating capital raising for
20 emerging and smaller companies.

21 So with that could I have a motion?

22 (Motion.)

23 MR. GRAHAM: Second.

24 (Second.)

25 MR. GRAHAM: Any more discussion? All in

1 favor.

2 (Chorus of ayes.)

3 MR. GRAHAM: Anyone opposed?

4 Okay, thank you. Do we have time for a break?

5 Okay, we don't have time for a break then. Annmarie.

6 MS. JACOBS: We're pleased to have with us
7 today Annmarie Tierney, executive vice president and
8 general counsel of Second Market Holdings. Second Market
9 is a leading provider of services to facilitate
10 transactions in private companies' stock. They have an
11 on line platform that provides a central market and
12 streamlined sales process of transactions in private
13 company stock, fixed income securities and bit coin.

14 Prior to joining Second Market Annemarie served
15 as general counsel and corporate secretary of NYFIX,
16 Inc., a NASDAQ public company and the assistant general
17 counsel at the NYSE Euronext. She also served as an
18 associate in the corporate finance group at the law firm
19 Skadden Arps and she began her legal career here at the
20 SEC as a senior counsel in the Office of International
21 Corporate Finance, in the Division of Corporate Finance.

22 Good morning and welcome.

23 MS. TIERNEY: Good morning. Thank you very
24 much. I'm delighted to be here. I like the new building
25 much more than I like the old building and I'm really

1 excited today to talk to you about what we're seeing in
2 secondary liquidity and talk to you about a piece of
3 legislation that we've been having some discussions on
4 the Hill regarding.

5 Okay. So just for those of you who may not be
6 familiar with Second Market, we have morphed over the
7 years in multiple ways. Our basic -- our premise has
8 always been to find liquidity for highly illiquid assets.

9 We have been in business since 2004. We're a registered
10 broker/dealer. We're based in New York City. And we've
11 completed about \$2.5 billion in transaction volume since
12 2013.

13 We got in the private company space around
14 2008. We had originally started trading restricted stock
15 of public companies, the preferreds and warrants and
16 things like that, morphed into a fixed income business
17 trading business, which is still a big business for us,
18 all trade securities and other highly liquid kind of bond
19 assets. And then as we kind of got a reputation in this
20 space we started getting phone calls from, really it was
21 Facebook, former Facebook employees or early investors in
22 Facebook saying you're finding liquidity for restricted
23 stock. Can you help us find buyers for Facebook stock?
24 And back then Facebook was not what it is now obviously.
25 It wasn't as well known.

1 But there was a big interest on the buy side
2 and we had a platform that was only available to
3 accredited investors, and we basically matched buyers and
4 sellers with Facebook stock and did that on a password
5 protected website where everybody who was able to
6 purchase was an accredited investor.

7 Once Facebook went public we started looking at
8 other types of companies that could also benefit from
9 secondary liquidity, and what we found pretty quickly was
10 that most private companies have no interest at all in
11 having unfettered secondary trading in their stock. They
12 care about who the buyers are, they care about the price
13 of the transaction.

14 Most of these companies have rights of first
15 refusal. They do not want -- I'm the general counsel of
16 a private company. I can tell you it is no fun to get
17 notices from shareholders saying I want to sell my shares
18 to Sarah or whomever else, and then we have to decide if
19 we're going to use our own money to buy the stock back at
20 that price or let the shares go to somebody that we may
21 not know. So it's a lot of administrative functionality
22 for the company.

23 So the way the product has morphed really since
24 2011 is that now in the secondary space we only provide
25 liquidity through private tender offers. That is what

1 companies want to be doing. There's a huge growing --
2 you'll see from -- do I have that -- oh, my gosh,
3 technology. Okay.

4 Being the general counsel of a technology
5 company I know I shouldn't say that.

6 So what we're seeing now is that in 2014 we
7 closed about \$1.4 billion in private tender offers on our
8 platform, which was a 400 percent increase since 2013.
9 And we're really seeing very dramatically the impact of
10 the JOBS Act, particularly the change, the 500
11 shareholder threshold, the increase to 2,000
12 shareholders, holders of record excluding employees.

13 That I think is borne out by the fact that we now
14 have about 73 venture backed companies in this space that
15 are valued at over \$1 billion, which is a significant
16 increase over the 13 that existed in that space in 2012.

17 So there's a real significant impact from the JOBS Act
18 that we're seeing every day.

19 MR. GRAHAM: Annemarie, sorry to interrupt.

20 MS. TIERNEY: Of course.

21 MR. GRAHAM: For some of us could you back up
22 and just kind of explain what you're achieving with the
23 private company tender offer.

24 MS. TIERNEY: Yes, of course. So basically
25 what -- and I'll skip to the bottom of the slide. So

1 basically what happens is the company engages us to act
2 as paying agent, depository agent and information agent.

3 We really are replacing the functionality provided by a
4 lot of law firms in this space, and law firms are our
5 biggest stream of business.

6 So basically the law firm says you want to run
7 a private tender offer. It's either a company buyback or
8 third party tender. In almost every instance the third
9 party investor is an institution the company locates
10 itself. We do not locate buy side interest anymore.
11 So the company says, okay, T. Rowe Price or Tiger
12 wants to buy shares in our company but we don't want to
13 do another preferred round potentially at this point
14 time, so we're going to allow those large institutional
15 investors to get a position on our cap table by allowing
16 our existing shareholders some liquidity.

17 What we see generally, and the great thing
18 about the product, is that the company basically controls
19 the entire process. They decide how often they want to
20 carve out liquidity. A lot of the larger pre-IPO
21 companies that we're dealing with are doing tenders maybe
22 twice a year, some are doing them every quarter. They
23 can decide who can sell. So my own company has done
24 tenders for our own shareholders three times, each time
25 with different parameters. The first time we allowed our

1 existing and former employees to sell 20 percent of
2 vested equity and our kind of initial investors were able
3 to sell as much as they wanted. In the second tender we
4 allowed only existing employees to participate. It was a
5 much smaller tender. And in the last one it was a third
6 party tender where we set the limitation at 30 percent.
7 So we really got to decide who bought the stock.

8 We brought in a big investor, institutional
9 investor, that subsequently did a Series C preferred
10 round. So we had a great new board member on our board
11 and a VC firm to help us grow to the next stage. Our
12 shareholders were delighted to get liquidity. We were
13 able to decide that we wanted to do the tender at a
14 premium to our 4(9)(a) valuation. And I think everybody
15 is probably familiar with the fact that in the private
16 company space a company gets an independent analysis done
17 once a year to set the price at which it issues equity to
18 its employees under its 71 plan. That's referred to as
19 the 4(9)(a) valuation.

20 And the more secondary trading there is the
21 more that independent third party has to consider that
22 trading when setting that price. So companies guard that
23 price very carefully.

24 So what we're seeing now is -- I'll go to the
25 next slide. The median valuation the company set of our

1 clients -- and I think we did about 40 private tenders
2 last year and we expect to do maybe closer to 80, 100
3 this year, median valuation is about \$950 million.
4 They've raised about \$158 million in capital. They have
5 about 300 shareholders on average. Most of them will be
6 employees or former employees. The median age is seven
7 years and the most common company that we're dealing with
8 is in the enterprise software space.

9 So these are names that you would know. We've
10 had a few companies who have been willing to kind of give
11 us testimonials. Sonos is one of them. We've done a
12 deal I think for Airbnb. So some really big pre-IPO
13 names that have -- Drop Box I think is the other one
14 that's publicly stated that we've done work for them.

15 So they are names that you would know, they're
16 companies that have an extremely large base of
17 shareholders. Most of them again are employees. IPO at
18 some point in the near future, but maybe not imminent.
19 Some companies will do a private tender offer to
20 clean up their cap table before they do an IPO. They may
21 want to get the cap table cleaned up. Again a lot of it
22 is just to keep employees feeling like their equity comp
23 is worthwhile to them.

24 I know as an employee of a private company a
25 lot of my compensation is in equity. I would like to buy

1 a house, go on vacation just like public company
2 employees. And so this is a way to give some liquidity
3 to employees of a company without actually letting them
4 go out 100 percent. So they keep some skin in the game
5 but they feel like they're actually getting value for all
6 the hard effort that they're putting into the company.

7 So with that does anybody have any questions
8 about kind of the secondary space as a general matter,
9 because I'm going to focus more specifically now on --
10 yes.

11 MS. LUNA: Some of the reading material for
12 this meeting had different numbers than what I'm seeing
13 in the slides. So I had -- I guess there was some
14 documentation about \$18 million was the median.

15 MS. TIERNEY: This came from our business team,
16 so I think what they gave is probably last year's report.
17 This is probably more updated numbers.

18 MS. LUNA: Okay. And that's a huge --

19 MS. TIERNEY: Jump.

20 MS. LUNA: -- jump from what I had. It was \$18
21 million and now it's, you know, depending on what line
22 item I should correlate it to its either \$158 or \$950.

23 MS. TIERNEY: So you're talking about the
24 median --

25 MS. LUNA: Yes, IPO.

1 MS. TIERNEY: Let me -- I'll check with our
2 business people and find out because they put the report
3 together for me and they also gave me these numbers.

4 MS. LUNA: Right. Got it.

5 MS. TIERNEY: But most of these companies are
6 very late stage pre-IPO. \$18 million is nothing. So it
7 sounds like \$18 million is definitely the wrong number.

8 MS. LUNA: Okay.

9 MR. CHACE: I think that's the transaction
10 size versus the valuation.

11 MS. TIERNEY: Yes, I think that was --

12 MS. LUNA: Oh, that's a different number.

13 MS. TIERNEY: Yes. Median funding raised, but
14 it's how much they've raised over the life of the
15 company.

16 MS. LUNA: Got it, okay.

17 MS. TIERNEY: And \$18 million would be the -- I
18 don't have the report in front of me, how much the
19 average tender offer was that's been done through our
20 platform. Thank you for -- I should have it with me.
21 I'm sorry I don't.

22 MS. LUNA: No worries.

23 MS. TIERNEY: Yes.

24 MR. HEMPILL: Are most of the holders of these
25 shares in these private companies subject to shareholder

1 agreements with rights of first refusal and limitations
2 on secondary transfers?

3 MS. TIERNEY: Yes, almost all of them do. And
4 that's another nice thing about the way that private
5 tenders work. The company waives all those limitations
6 in advance of the tender commencing, and most of the
7 employees make exercise of their options conditional upon
8 the closing of the tender. Because again when I'll talk
9 about this concept of 4(a)(1-1/2) in a second, it's
10 really tied to how do you pay for option exercise in the
11 context of these securities where you don't have 144
12 available to you.

13 So what we're seeing is conditional option
14 exercise where the people know for sure that the tender -
15 - because some of the tenders are pro-rated. Sometimes
16 there's more buy side -- more sell side interest than buy
17 side interest. So there's sometimes pro-ration across
18 all the participants.

19 MR. HEMPILL: And do you see the opposite where
20 in fact if the tender offer has a stated notional amount
21 of \$25 million and you're limiting it to 20 percent of
22 holders of a certain class if there's undersubscription
23 where people might be able to over participate given the
24 aggregate limit?

25 MS. TIERNEY: I think generally speaking the

1 tenders are fully subscribed on both sides. I don't have
2 any specific facts about things that were under. We've
3 had one deal where the company was a buyer next to some
4 third parties and if there was too much sell side
5 interest the company was willing to pick up more than was
6 originally the maximum of the tender. So we've really
7 seen generally more sell side interest, but definitely
8 matched by buy side interest.

9 And because these are fully negotiated deals
10 before they commence there's not a lot of room for
11 surprise. They know how much maximum potential sell side
12 interest is and they know how much the maximum buy side
13 interest is, and that's fully disclosed in all the tender
14 offer documents and these transactions are well
15 documented. There's an offer to purchase, there's a
16 letter of transmittal, there's diligence materials
17 provided to the participants. So it's a fully compliant
18 -- tell me -- it's 14(e), right? I'm not an M&A lawyer,
19 but 14(e) private tender offer. So open for 20 business
20 days and all the rest of it.

21 MR. HEMPILL: And why the move from the law
22 firms handling these to your company handling these?

23 MS. TIERNEY: Our price point is really
24 competitive and law firms love looking like they're
25 helping their clients save money. When we developed the

1 product we did it with law firms. We always wanted to be
2 a service provider to companies and their firms.
3 What the law firms said to us was this was kind of
4 the thing where we send a paralegal or first year into a
5 room with boxes of documents and they have to review
6 every single signature and make sure things are filled
7 out properly. Our entire product is done electronically.
8 So you sign onto the web -- you sign onto the platform.
9 You'll see exactly what you hold an you'll see exactly
10 what you can sell.

11 And then you complete a profile page that auto
12 populates a letter of transmittal with your sell order.
13 So you can't actually make mistakes. If your spouse
14 needs to sign it, it makes you get a spousal consent. So
15 it's almost a foolproof method of letter of transmittal
16 completion along with any other documents that the
17 company wants signed in the context of the transaction,
18 like a new right of first refusal agreement, or a
19 shareholder agreement, or that sort of thing.

20 So law firms were telling us that they were not
21 able to bill a lot of this time to their clients, so they
22 were writing it off. So for us to come in and do it --
23 we generally charge a minimum of \$25,000 or \$250 per
24 eligible participant. So for a really large tender offer
25 maybe our fee is \$125,000. It's still significantly less

1 with 6 or 700 potential sellers, much less than the law
2 firm is going to charge.

3 So law firms are -- that's how we market the
4 product is through law firms. We don't generally deal
5 directly with companies. We have a handful of law firms
6 that are very active in the private tender space and
7 that's where we spend all of our marketing time.

8 MR. HIGGINS: Are the sellers typically
9 employees?

10 MS. TIERNEY: They typically include employees,
11 but they're the whole range of potential investors. So
12 they're Angel investors, they are former employees,
13 they're current employees, and they could be founders,
14 the whole panoply. And again the company may decide this
15 tender is only open to current employees. So it's really
16 up to the company. But generally speaking we see
17 availability, participation across the entire shareholder
18 base.

19 MR. SAADE: I have a couple of questions.

20 MS. TIERNEY: Sure.

21 MR. SAADE: Have they always been up rounds?

22 MS. TIERNEY: Have they always been up rounds
23 in what sense?

24 MR. SAADE: In the --

25 MS. TIERNEY: The company is not actually

1 raising capital here.

2 MR. SAADE: No, I understand. But are
3 employees willing to sell at a valuation that's lower
4 than before, that the companies have preemption as to
5 what the valuation -- does it always have to be a higher
6 valuation than the last one?

7 MS. TIERNEY: Well, I don't know the answer to
8 that question because companies' 4(9)(a) valuations can
9 fluctuate from year to year. So maybe one year it's 10
10 and then next year it's 15, but the next year it could be
11 7. Normally the private tender is priced at some type of
12 premium to the 4(9)(a) valuation because where a recent,
13 maybe a recent preferred round closed. So they're always
14 pricing off of another valuation metric. And again these
15 are completely voluntary. People do not have to sell
16 their stock at this price. There's lovely pages of risk
17 factors that the company's price could be higher or
18 lower. It just depends.

19 MR. SAADE: And then on the percentage of your
20 business that's stock versus warrants, are you also
21 trading on warrants and calls and puts on options?

22 MS. TIERNEY: So we don't trade at all. The
23 product is purely facilitating private tender offers.
24 We're not an exchange, we're not an ATS, we're not a
25 bulletin board at all. We are -- it's the most simple

1 product, and that's what people can't get their head
2 around sometimes knowing what we used to do that and this
3 is what we do now. We're literally acting as a service
4 provider to close private tender offers.

5 Lots of companies will say if you have options
6 or warrants you can convert those in the context of the
7 private tender, but most buyers are buying the underlying
8 common. They're not looking to buy warrants or preferred
9 -- warrants or common. A lot of the tenders include
10 preferred as well. It just depends again on what's the
11 interest of the potential buyer, if it's a third party,
12 and what are they looking to achieve by the investment.

13 Okay, I'm watching my time because -- okay. So
14 let me know if I'm going too long. Okay.

15 So where we are -- so over the history that
16 we've been in the private company space we've been pretty
17 active. We were pretty active in the JOBS Act on the 500
18 shareholder threshold and general solicitation, and after
19 the JOBS Act passed we were approached by some of the
20 people we worked with on that legislation for other areas
21 of potential legislation that could also facilitate
22 capital raising. And what we started focusing on was the
23 fact that there is no federal exemption for secondary
24 transactions other than 144, which requires in the
25 private company context that the stock -- that common

1 stock generally be held for 12 months. It's also not
2 available to affiliates.

3 And where we started really focusing on that
4 was as I said earlier once Facebook went public and we
5 started focusing on other groups of companies that we
6 could provide liquidity for, we started focusing on
7 private community banks. And we did that because the
8 flip side of the 12(g), you know, increase of
9 registration threshold was a decrease to allow private
10 community banks to de-register more simply.

11 And so we spent about 18 months looking at
12 private community banks and trying to figure out how to
13 create liquidity. Somebody made the comment earlier that
14 there's a real correlation for companies if their buyers
15 know that they're going to be able to get some kind of
16 liquidity at some certain point in time other than an
17 IPO, it's much easier for these companies to raise
18 capital. And we heard that over and over and over again
19 from community banks. If we can tell investors, yes,
20 we'll provide you liquidity in a year, or six months, or
21 whenever, it was going to be much easier for them to
22 raise capital.

23 The problem that we found in those contexts
24 were most bank's officers and directors obviously are
25 affiliates and they're precluded from relying on Rule 144

1 in any context. And a lot of these people have been
2 managers for banks a long time. These are not wealthy
3 people. They're just, you know, local bank managers.
4 They are comfortable probably, but they're not wealthy,
5 wealthy. But they didn't understand why we couldn't help
6 them find buy side interest.

7 And the reason that we couldn't find buy side
8 interest, and I'll skip ahead for a second -- is this.
9 The states -- because there's no federal exemption that
10 is available to people who have held for less than 12
11 months or for an affiliate of a private company. We had
12 to look at the Blue Sky requirements in all 50 states.

13 And again we're a registered broker/dealer.
14 The way that FINRA and SEC rules work are if we
15 have a substantial preexisting relationship with a client
16 we can market to that client. We could say, okay, in a
17 primary context here's a community bank that you may want
18 to invest directly in.

19 In the secondary trading sense that doesn't
20 apply. In fact what the state's exemption says here is
21 that a transaction is only exempt under state law if the
22 bid is unsolicited. Now what does that mean?
23 So we went to the State of California and we said
24 here's the way our platform worked at the time. You had
25 to sign up on Second Market. You had to go through

1 accreditation, you had to go through -- know your client
2 in AML. You had to tell us that you wanted to buy
3 private company stock. You might also tell us that you
4 want to buy stock in the State of California. Was that
5 sufficient nexus to allow us to let that potential
6 investor know that there were shares for sale in a
7 California community bank? And the State of California
8 said no. Even those many steps does not create a
9 situation where you can market that opportunity to
10 investors in the State of California.

11 And so what we realized was private community
12 banks particularly wanted investors that were local to
13 the bank. Maybe a New Jersey bank wanted investors from
14 new Jersey Pennsylvania and New York. We could not
15 create one size fits all liquidity for that bank in those
16 three states. The different state laws were so
17 conflictive. So we ultimately gave up the community bank
18 space. I saw some news recently that OTCQX is looking at
19 some kind of community bank exchange, which I think will
20 be a phenomenal help to community bank capital raising if
21 they can solve it for this problem.

22 But what we ended up doing was giving up the
23 community bank space and started talking about the need
24 to codify what's referred to as 4(a)(1-1/2) now. And
25 what that is is a construct of law that's developed since

1 I think the 50's with the Ralston Purina case and more
2 case law after that, and legal interpretation and opinion
3 practice, and basically 4(a)(1-1/2) now says that if you
4 meet certain parameters that are sort for 1 and sort for
5 2, that you're deemed to be exempt under federal law for
6 second transactions where the buyer is accredited,
7 there's no distribution, and certain other parameters are
8 met.

9 So what we started saying was to the people on
10 the Hill that we had been asked to talk to for other ways
11 for capital formation facilitation, this is a place
12 that's really important. You see that companies are
13 staying private much longer. They have significant
14 shareholder bases. Any employee who has options can
15 never rely on Rule 144 to pay for the option exercise.
16 They have to have cash at the time that they're
17 exercising options to pay for the option exercise price
18 and the taxes that become due. These are rank and file
19 employees who cannot afford to do that out of pocket.
20 So what we started to see is kind of problematic
21 practices popping up, almost like pay day lenders where
22 people are lending employees money to exercise options
23 and then sell the common stock. It's not a good
24 practice, and I think it's probably pretty unnecessary,
25 and a lot of employees are getting ripped off. That's my

1 opinion and also the opinion of Second Market. And I
2 don't have to give a disclaimer.

3 So what we started seeing was the states have -
4 - and we've been talking now so I'll -- you know, we have
5 a great relationship I believe with NASAA. We've been
6 talking with them for about 3-1/2 years about the need
7 for another way to facilitate secondary trading at the
8 state level. I don't think that they're going to be able
9 to adopt similar legislation in all 50 states, and if
10 they do it's going to be the same problem with all of
11 these other exemptions, which there's an isolated non-
12 issuer exemption for secondary trading, there's an
13 institutional exemption for secondary trading. Maybe a
14 majority of states will have the same wording, but not
15 every state interprets the number of how many is non-
16 isolated the same. Some of them exempt affiliates from
17 alliance. It's just a complete patchwork that's
18 unworkable even for a broker/dealer who put two years
19 into trying to figure it out.

20 So our position is that it's time for the SEC or
21 Congress to do a federal exemption for secondary trading
22 for shares that have been held for less than 12 months
23 and for affiliates. Basically the legislation that we've
24 been talking to different people about is provided in
25 your packages.

1 The first bill that we were talking to Congress
2 about passed the House Financial Services Committee last
3 spring, but it included some provisions that were
4 problematic to the SEC it was my understanding, and also
5 to the Democrats on the House Financial Services
6 Committee. So this bill has been amended to address
7 those concerns. And we have I think two sponsors, right,
8 a Democrat and a Republican in the House who are willing
9 to sponsor this legislation hopefully this year. There's
10 some talk of a JOBS Act 2.0 kind of perking around and
11 this could be something that we add into that.

12 So that's sort of where we're seeing the need.

13 Let me think if I missed anything.

14 You know, one thing that's really important to
15 think about and what we've talked, spent a lot of time
16 talking to states about is investor protections here.

17 Securities have been -- that are eligible for sale under
18 4(a) (1-1/2), the buyers have to be accredited investors.

19 And what doesn't make sense to me specifically is that
20 state law doesn't apply to how the majority of these
21 securities were issued, right, 506(b) or (c), Rule 701,
22 so states didn't have jurisdiction.

23 There was preemption when the securities were
24 issued, but in the secondary context there's no
25 preemption and that I think is problematic. And I've

1 talked to Bill Beatty who is the current president of
2 NAASA. He and I think testified in front of the House.
3 And I said to Bill, "You're not allowed to say that you
4 hate the legislation." He's like, "Okay, I won't." But
5 he was talking about Reg A, and I had to try to hold my
6 tongue on that one.

7 But I think the time has come. The SEC has not
8 done I think much on 41 since 144, and they haven't been
9 at least historically open to more no action letters in
10 this space. We tried a few years ago to get some kind of
11 guidance on option exercise and immediate resale of the
12 common, but the staff didn't think it was the right time
13 for that.

14 So this is sort of where we're heading, and
15 like I said the messages are pretty easy. There's no
16 real investor protection issues here. The states have
17 been pretty open that this is not an area where they've
18 seen problematic practices. This is not a place where
19 states have filings made. So the idea of like imposing
20 filing requirements doesn't make any sense to us. Hold
21 time again would make the whole thing fall apart because
22 of the option exercise and the need for the immediate
23 payment on the exercised side.

24 So I think we're pretty proud of the
25 legislation and we're proud of the people in Congress

1 that we're working with who are supporting it, and I'm
2 also really grateful to the SEC for all the listening
3 they've done on me going on about this for how long, in
4 some fashion for 18 months.

5 So that's it. Anybody have any -- I talked
6 really fast and I've been watching the clock so I
7 apologize. I have my New York speed going.

8 MR. PAUL: I hate using these things, and
9 usually my voice carries, but okay. Do you feel that
10 it's necessary for this to be handled legislatively or do
11 you believe that this can be handled here at the SEC by
12 regulation?

13 MS. TIERNEY: I would love to see the SEC take
14 this up. I think they would be able to do it justice. I
15 think it's not that controversial.
16 My concern would be the length of time it will take
17 to get through and the idea, and I'm sorry, I don't mean
18 to disparage the Commission in any way, but I watched
19 what happened with general solicitation and the proposed
20 Reg D changes that basically -- Dan knows how I feel
21 about this one -- how that basically makes people -- it's
22 going to make people rethink utilizing general
23 solicitation with the proposed changes. So additional,
24 you know, Reg D filings and filing information with the
25 SEC and other kinds of investor protective provisions are

1 loaded onto this. It's a really simple concept. Legal
2 opinions are written about this every single day. My
3 only concern is that there will be a different contingent
4 with a different view who want to build in some kind of
5 hold periods or filing requirements, which again make no
6 sense. So that's my only concern about the process if
7 the SEC were to pick it up. But I would love to see the
8 SEC pick this up and put it out for public comment.

9 MR. GRAHAM: John.

10 MR. HEMPILL: I really appreciate your
11 presentation. It was very informative.

12 MS. TIERNEY: Thank you.

13 MR. HEMPILL: One question I have, any thought
14 about -- you know, you mentioned that oftentimes the
15 sellers are employees exercising options. Any thought
16 given to in this proposal here about some requirement on
17 who the seller is, in other words that they have a
18 certain level of sophistication as well?

19 MS. TIERNEY: Well, they got the shares. So --

20 MR. HEMPILL: Yes, but they're also selling the
21 shares into a marketplace where they --

22 MS. TIERNEY: It's not a marketplace. So again
23 there's -- right, there's no exchange here. So I think
24 we have to be -- I know that there's an idea that there
25 should be a venture capital exchange, which I think is

1 really, really important. But here these are employees
2 of the company who have been working for the company
3 generally at least the four years it takes for options to
4 vest. They have protections under Rule 701 when they
5 exercise their options. They have to be provided certain
6 disclosures, like financial statements and other
7 documentation. So protections from the seller against
8 their own employers I think are all baked into the
9 product.

10 MR. HEMPILL: Not against their employer but
11 against the purchaser. For example in bankruptcy, when
12 you're selling bankruptcy claims, actually the focus is
13 on whether or not the seller is getting sufficient
14 disclosure from the buyer, because the presumption is
15 that the buyer has better position, more information than
16 the seller does. And given the likelihood here that you
17 have some 23 year old kid liquidating their options and
18 selling it prior to the IPO is that something that you
19 think is a concern?

20 MS. TIERNEY: I don't think it's a concern.
21 These transactions are fully -- are fully regulated under
22 the 33 Act. I mean, there can't be --

23 MR. HEMPILL: Getting the securities is,
24 including when they get the option.

25 MS. TIERNEY: The sale, the sale is covered by

1 the anti-fraud and all the anti-fraud and insider trading
2 rules of the 33 and 34 Act. So if the buyer is buying on
3 inside information that's illegal. They have to either
4 make the disclosure available to the sellers, which is
5 what most of those companies are doing, they're providing
6 disclosure that puts buyers and sellers on equal footing.

7 But in 60 percent of the cases it's the company buying
8 back its own stock because it wants to find liquidity
9 with shareholders.

10 It's not meant to be a way to cheat their --
11 again these are employees of the company. The company is
12 incentivized to make them happy and help them want to
13 stay at the company and feel like they're productive
14 members of the company's employee base. So we haven't
15 seen any bad practices like that at all.

16 And in fact a lot of companies -- when we did -- I
17 can give you an example of my own company. When we did
18 our first private tender we had a third party buyer. My
19 CEO was selling some shares and the document that we
20 provided to the buyers and sellers was almost -- you
21 know, I'm former public company lawyer. I can't help
22 myself. It was very robust, like so much more robust
23 than my CEO was comfortable with.

24 But I'm like, listen, you're selling. We have
25 to put everybody on even footing. And you know these are

1 regulated transactions even though they're exempt.

2 MR. HEMPILL: Yes. So, you know, in the
3 example you gave there was robust disclosure. So again
4 just given kind of the nature of the seller base do you
5 think there should be some sort of disclosure requirement
6 perhaps?

7 MS. TIERNEY: No, because not all these
8 transactions will occur in a private tender and a lot of
9 sellers have no legal -- no legal rights to information,
10 or if they have legal rights to information they're
11 precluded from sharing them with third parties. So the
12 idea of imposing -- there's no information required in a
13 506(b) or (c) offering. There's no information required

14 MR. HEMPILL: Right, but you have accredited
15 investors in those circumstances.

16 MS. TIERNEY: These are accredited investors
17 too. All the buyers in this case are accredited.

18 MR. HEMPILL: The investors are, but not the
19 sellers.

20 MS. TIERNEY: I mean, I don't know if they're -
21 - again if they're exercising options they are provided
22 disclosure under Rule 701. So I don't really understand
23 why you think they're not protected from an information
24 point of view.

25 MR. HEMPILL: Well, I mean, the disclosure

1 under 701 is not that robust.

2 MS. TIERNEY: Well, it's as robust as you're
3 going to get as an investor in a Reg D offering.

4 MR. HEMPILL: Well, there's no -- in a 506
5 offering there's no -- if you're selling on to accredited
6 investors there's no minimum disclosure requirement
7 outside of anti-fraud.

8 MS. TIERNEY: Correct. But most companies
9 provide disclosure, otherwise people aren't willing to
10 invest in them.

11 MR. HEMPILL: Anyway, maybe it was just a --

12 MS. TIERNEY: No, see the question --

13 MR. PAUL: Your concern then is that the seller
14 being a non-accredited investor, an employee that
15 accumulated the shares probably in lieu of a decent
16 salary is going to get picked off by the accredited
17 investors who are buying them?

18 MR. HEMPILL: Yes. They're more sophisticated.

19 MS. TIERNEY: But again they're approved by the
20 company to participate in our market, so the company is
21 looking out for the best interests of employees almost
22 exclusively as the reason they're doing the tender in the
23 first place. They know that they're not going public for
24 a period of time. They have an employee base with no
25 access to liquidity, transfer restrictions, you know, in

1 the form of rights of first refusal and other transfer
2 restrictions. So the only way that these people are
3 getting liquidity is through these types of transactions.

4 I think the other thing that's really important for you
5 to understand is that when you leave a private company
6 you generally have 30 to 60 days to exercise your equity
7 or it expires, and if these people cannot find the cash
8 to pay for that then they've lost the value of 60 percent
9 of their compensation for no good reason.

10 MR. HEMPILL: Right.

11 MS. TIERNEY: So I think that's another thing
12 to really keep in mind.

13 MR. REESE: I would like to add to that my own
14 personal story where we had employees -- we used stock,
15 equity stock options as an incentive in our company. And
16 the sophistication amongst employees in understanding
17 what that is has grown tremendously, because at the time
18 folks didn't understand what it meant, because it's not a
19 liquid asset.

20 MS. TIERNEY: Right.

21 MR. REESE: It's not something they can go buy
22 baby food and pay their car note. So it is important to
23 have salary, but we made it an important part of the plan
24 to have you get a good salary, you get a competitive
25 salary, you get -- you got a 401(k) plan and -- but what

1 we felt was important because we were a fast growing
2 company is to give you a piece of the pie.

3 MS. TIERNEY: Right.

4 MR. REESE: And it's important because have you
5 -- if you don't have an ability to have an exit or if you
6 want to delay an exit you can lose your employee base
7 amongst the brightest and smartest if they don't see --
8 because somebody would pay them a few dollars more in
9 their salary or their equity is liquidable in another
10 company, I did see that type of issue. So I think this
11 is -- from my own standpoint I think that's a fabulous
12 opportunity, and listening to John and trying to
13 understand about the option plan I think where everyone -
14 - every employee -- we had our -- we had Merrill Lynch
15 handle our plan and we had our lawyers advise. But with
16 the signing on of your employee they get their option
17 plan as a full plan as part of their employment package.

18 And so that's -- it should have some rules and
19 regulations whatever that is. I didn't even read it at
20 that time.

21 MS. TIERNEY: That's great.

22 MR. REESE: But I don't think --

23 MS. TIERNEY: I bet your lawyer appreciates
24 that.

25 MR. REESE: But I had my lawyer. But I think

1 what the point is is that it doesn't mean anything to
2 them.

3 MS. TIERNEY: No.

4 MR. REESE: What I'm trying to say is something
5 that you don't spend means very little until you do have
6 an opportunity to spend it. And the fact that if you can
7 create income on top of what you've already had and be
8 able to pay the -- I thought the key things are taxes and
9 the fact that you have a taxable event to yourself.

10 MS. TIERNEY: Right. And so it's -- you have
11 to pay the cost of the exercise and its income tax.

12 MR. REESE: And you still have money -- and the
13 idea is you still have money left over --

14 MS. TIERNEY: Left, exactly.

15 MR. REESE: -- to pay and put it against a house
16 and things of that nature.

17 MS. TIERNEY: Correct.

18 MR. REESE: So very, very critical issue to me.
19 I see it in multiple companies that I've dealt with and
20 invested in. And I think that's an important -- this is
21 an important regulation that needs to be solved that can
22 free up a lot of capital in a lot of states.

23 MS. TIERNEY: When we talked to the states the
24 things that we talked about -- I presented to NAASA's
25 board about two years ago this May and then I got a

1 Chace to speak at their annual conference a couple of
2 years ago, and the point that I think that's important to
3 keep in mind is that again there's no problematic
4 practice -- these transactions already happen every
5 single day. Law firms are writing 4(a)(1-1/2) opinions
6 every single day. So it's not a new concept at all.
7 It's a tried and true concept.

8 Companies will have the same exact control over
9 the transaction they have now even if this legislation
10 was passed. The legislation is very non-controversial.
11 It just codifies existing opinion practice. I got the
12 input of I think probably 20 different securities lawyers
13 at this point, including some people at this table with
14 white and red -- blonde and red hair -- and when we
15 talked it through we were looking at all the issues that
16 could come up.

17 And we wanted something again non-
18 controversial, reflecting current opinion practice. What
19 this does is just allows easier location of buy side
20 interest for unknown companies. It's super easy to find
21 buyers of Facebook, its super easy to find buyers of
22 well-known pre IPO companies. It is not easy to find
23 buyers for community banks, it is not easy to find buyers
24 of unknown tech companies, bio, you know, maybe bio
25 companies or in Boston. Like those companies have a lot

1 of trouble finding buyers.

2 If a broker/dealer can't locate buy side interest
3 the same way it can in a primary sense that just doesn't
4 make any sense to me. So I just keep coming back to the
5 economy of practice between primary and secondary is
6 unnecessary in this point in history, and it is really an
7 impediment to capital formation. If you can find buyers
8 for secondary shares you are going to facilitate primary
9 capital raising. It's pretty basic.

10 What the states wanted to talk about was what
11 it -- so the impact to the state is income tax when the
12 options are exercised and capital gains tax when the
13 common is sold. It's a huge tax benefit to the states in
14 an area with non, you know, no known problematic
15 practices. And Jan Owens who is the Commissioner from
16 California said, "Well, Annemarie, what does that mean?"
17 And I said, "Well, Jan, in like 2010 and 2011 we
18 sold \$484 million worth of Facebook stock for California
19 residents. California doesn't have an income tax but
20 they certainly have a capital gains tax, so that's a big
21 upside for the State of California."

22 And again the idea that if you are leaving a
23 private company and you have a significant compensation
24 element in equity that's going to expire within 30 to 60
25 days, that's a huge impact on your community. That's

1 money that's not going to be in your pocket to buy a
2 home, or a car, or put your kids through school. And
3 there is again no real reason for that to be occurring in
4 the kind of environment that we're in right now, where
5 companies are going to stay private longer. It's just
6 the reality after the JOBS Act.

7 MR. HEMPILL: So just one question. So these
8 programs are put into place by you with the company so it
9 can be done on kind of a regular basis so that any
10 employee that leaves can take advantage of this?

11 MS. TIERNEY: Not at all. Absolutely not.

12 MR. HEMPILL: No?

13 MS. TIERNEY: Our product is based on what the
14 company -- we are not a stock exchange.

15 MR. HEMPILL: No, no, no. I understand that.

16 MR. TIERNEY: We are doing private tenders and
17 private tenders are generally done once a year, twice a
18 year, three times a year. This legislation goes much
19 further than private tender offers. It's something that
20 will impact the entire market, not Second Market
21 specifically. It will just take another element of
22 confusion out of an equation where it's unnecessary.

23 MR. HEMPILL: Yeah. No, my question was really
24 about -- you keep on mentioning the 60 to 90 day window
25 after the employee leaves.

1 MS. TIERNEY: If I leave Second Market today
2 I've got 60 days to exercise my option.

3 MR. HEMPILL: No, I understand that, I
4 understand that. But when --

5 MS. TIERNEY: And there's no liquidity program
6 at my company right now. That means I'm going to have to
7 come up with cash out of my own pocket to pay for the
8 exercise costs.

9 MR. HEMPILL: I understand all that stuff. My
10 question is is that so this -- this enables the company
11 to provide that type of liquidity to any departing
12 employee?

13 MS. TIERNEY: Provides the shareholder --

14 MR. HEMPILL: Right.

15 MS. TIERNEY: -- to find liquidity for its own
16 shares.

17 MR. REESE: It's not an individualized sell. I
18 think you -- it could be, but I think you have to set it
19 up, the company has to set it up. I think what John's
20 asking is maybe if you just breakdown the difference
21 between the two.

22 MS. TIERNEY: So let me interrupt you for a
23 second. That's Second Market, right. So this legislation
24 would allow a venture capital exchange to form, to be
25 created where actually shares could trade in that venture

1 capital exchange that are not capable of being traded in
2 that concept right now because they haven't been held for
3 12 months. So there's this concept that you want a
4 venture capital exchange, but what are the shares that
5 are going to be traded on there.

6 The only shares that are eligible to be traded
7 right now are shares that have been held for more than 12
8 months under Rule 144. That is maybe, I don't know, what
9 would you guess, 10 percent of the outstanding market in
10 private company stock? 97 percent of what we see is
11 stock that's held in the form of options that could not
12 be exercised and sold on the venture capital market if
13 this legislation is not in place.

14 MR. GRAHAM: Greg.

15 MR. YADLEY: Yes. I don't think anybody,
16 Annemarie, is objecting to what you all are doing, and
17 this may be a question for Mike. Just trying to read
18 this, who else would this apply to and what are the
19 protections? I think that was John's major forum. So
20 you've got some baked in here. One is that there can't
21 be some professional making a commission so they're out -
22 - so that there's an incentive.

23 MS. TIERNEY: Correct.

24 MR. YARDLEY: And the other is no general
25 solicitation. So --

1 MS. TIERNEY: And the buyer has to be
2 accredited.

3 MR. YARDLEY: -- presumably there's some
4 relationship here. When the states have looked at it is
5 that sort of how you've reviewed this too? Because, I
6 mean, I think this sounds terrific and the only thing I'm
7 sort of reflecting on John's question and trying to see
8 how -- is there an unintended transaction here that could
9 harm the seller?

10 MS. TIERNEY: Well, I -- you know, we all know,
11 let's be realistic, there's always a Chace for bad
12 behavior in every single aspect of securities law. So I
13 can't answer the question. It's not something we're
14 seeing. It's not something that from my knowledge of
15 what Bill Beatty and Mike Canning have told me. This is
16 not an area where the states are seeing problematic
17 practices, and it's something that's happening every day.

18 You know, right now in order to sell secondary
19 shares -- to sell shares in a secondary transaction
20 sellers are getting a 4(a)(1-1/2) opinion and a Blue Sky
21 opinion. They're getting them every day. So, right, you
22 probably are closer to it than I am, and I don't know
23 what elements you look at in order to issue those
24 opinions. But this -- all this does is sets -- creates a
25 safe harbor to do a 4(a)(1-1/2) transaction. It's not

1 the only way to do it, you could do it other ways, but it
2 just takes the state law friction out of locating buy
3 side interest. That's rally all this is intended to do.

4 MR. CHACE: Could I just ask, what's the
5 typical financial disclosure in the deals?

6 MS. TIERNEY: In our deals?

7 MR. CHACE: Yes.

8 MS. TIERNEY: Two years of audited financial
9 statements. It's basically 701 type information plus.
10 It depends -- corporate documentation, its generally risk
11 factors along the lines of if you sell your shares now
12 they might be worth more later.

13 MR. CHACE: But two years of audited financial
14 statements?

15 MS. TIERNEY: If the company has been in
16 business that long, yes. Most of the companies as the
17 slide indicated have been in business for seven years, so
18 almost every single company we do business with is
19 providing two years of audited financial statements and
20 interim financial statements.

21 MR. GRAHAM: Charles. Charles.

22 MR. HIGGINS: Just to follow up, but just to be
23 clear that's because the companies choose to do that,
24 there's no --

25 MS. TIERNEY: Correct.

1 MR. HIGGINS: -- there's no statutory or
2 regulatory requirement --

3 MS. TIERNEY: Right.

4 MR. HIGGINS: -- that they do it. They just do
5 it for 10(b)(5) purposes probably to protect themselves.

6 MS. TIERNEY: Right. That's exactly right.

7 MR. BALTIC: Thank you, Annemarie, for the
8 presentation. Very interesting concept and easy way and
9 elegant way to provide liquidity to private investors.

10 I had maybe a factual question. I think you
11 mentioned that this really would be a vehicle to the
12 proposed 4(a)(7) to codify existing opinion practice.
13 And I was just curious as to whether you had a
14 perspective on that practice or maybe an opinion as to
15 whether this was equally applicable for different types
16 of companies at different points in their capital
17 raising.

18 And I just point -- you mentioned earlier bio
19 Technology, it may be very different for instance for a
20 bio technology company private versus a private
21 technology company, where that company might be with
22 respect to how much capital it will need to raise going
23 forward, perhaps many, many rounds as a private and maybe
24 potentially public company versus a technology company,
25 which would be maybe much closer to revenues or already

1 generating revenues as a private company or even
2 profitable as a private company.

3 So I'm just wondering if you have any sense of
4 whether the opinion practice varies at all with respect
5 to the types of companies and where in the capital
6 formation curve they are or whether you have an opinion
7 or Second Market has an opinion about that.

8 MS. TIERNEY: So I left private practice in
9 2002, so I don't know what current opinion practice is in
10 most large law firms. There are obviously lawyers who
11 would probably be able to give you more information. But
12 I think what we're seeing is the analysis is the same no
13 matter what the company is. The analysis depends on
14 factors like there's no distribution, there's -- bios are
15 accredited investors.

16 You know, generally information is available on
17 the transaction or it's not depending on who the
18 participants are. There could be a big boy letter that
19 protects the buyer and the seller or vice-a-versa.
20 Nobody is interested in a situation where there's
21 rescission rights at the end of the transaction.
22 So people are very conscious of the idea that
23 there's rescission rights -- if there's a -- you know,
24 quality of information. So not to my knowledge is there
25 a different practice.

1 You know, part of what's inherent in 4(a)(1-
2 1/2) that I do see applied differently is this concept a
3 hold period. Some law firms don't think that a hold
4 period is a critical factor to the analysis and some
5 firms do. In the cases where we're working with
6 companies where firms think that it's critical that there
7 be some kind of hold period, the companies are actually
8 making their employees pay for the option exercise out of
9 their own pocket prior to the completion of the tender,
10 which just seems like a straw transaction. That makes no
11 sense to us. A lot of times they're writing a check --
12 don't listen please -- that's not actually cashed or
13 they're signing a promissory note. But, you know, it's
14 the reality of it.

15 Or we're seeing these problematic practices
16 develop where they're going out to a third party lender,
17 doing some kind of weird derivative swap that once they
18 can pay for the option that third party gets the rights
19 to the common, sometimes in violation of transfer
20 restrictions.

21 So we're hearing from more and more law firms
22 that they're seeing that as a problematic practice.

23 MR. BALTIC: And just to follow up, one of the
24 reasons I raised it, and it ties maybe back a little bit
25 to maybe what John was getting at is that, you know, for

1 certain types of companies where there aren't maybe
2 established financial metrics that you can hang valuation
3 on it becomes much more difficult to provide a valuation
4 and valuation becomes much more subjective and probably
5 much more volatile. So I can see that in some early stage
6 companies without really any financial metrics like
7 revenues there's certainly probability that the valuation
8 question and protecting sellers as employees maybe more
9 poignant of a question. So that's one of the reasons I
10 raised it.

11 MS. TIERNEY: That's an excellent question. I
12 think in our planet at least these companies have been in
13 business for at least seven years as a general matter.
14 They have a critical mass of shareholders. It's not
15 worth the company's time or efforts to put together a
16 private tender offer unless -- we generally see companies
17 who have at least 300 shareholders or are generally
18 looking to provide some kind of liquidity. Because
19 that's probably a pretty pent up employee base that's
20 held stock for at least four years and potentially
21 longer.

22 So I think it would be atypical for an early
23 stage company to utilize 4 (1-1/2) in the existing
24 opinion practice. I think it's probably hard to locate
25 buyers for those types of companies in a secondary

1 context. It's hard enough to raise money from a primary
2 context, so I don't know how you them find buyers. The
3 broker/dealers that are out in the market, if the seller
4 was utilizing a broker dealer that was familiar with the
5 space, they probably would have more success finding a
6 buyer.

7 But it's really I think slightly older, larger
8 based companies that are finding liquidity to be a good
9 option for them pending a decision to go public someday.

10 Otherwise I think bio tech companies, and again I'm not
11 a practicing attorney, a practicing law firm attorney, I
12 think more bio tech companies are probably waiting longer
13 to go public based on the product that they're developing
14 and what their model is. But I don't know for sure.

15 MR. GRAHAM: Okay, Milton.

16 MR. CHANG: Maybe I missed the nuance. It
17 seems like currently if you want to sell -- if you are an
18 employee and you want to sell 14(b) stock you go to your
19 company and you say I got some stock to sell, can you
20 help me to find a buyer. And then you got to get the
21 lawyers concurrence, et cetera, et cetera. And you seem
22 to have systemized the system but you're not doing
23 anything new. Did I get that right?

24 MS. TIERNEY: We're not actually -- the
25 securities are generally not 144 eligible. So that's the

1 most important factor in your fact pattern.

2 MR. CHANG: Oh, okay.

3 MS. TIERNEY: The vast majority of the
4 securities are held in the form of options that are
5 exercised at the point of the tender offer. So they're
6 not eligible Rule 144. And most companies don't let their
7 employees just come and say I want you to find me a buyer
8 because the company has to be very careful about locating
9 buyers because they don't want to be, deemed to be part
10 of a distribution.

11 So I think depending on the company they're
12 probably just prohibiting transferability until an IPO or
13 they're providing this interim liquidity. Alibaba did
14 this themselves before they went public. They did a big
15 third party tender offer with like thousands of
16 participants. It didn't happen through Second Market. I
17 think they used a law firm to do it. But they basically
18 gave people an opportunity to get some liquidity for
19 restricted stock before the company did an IPO.
20 And so we're seeing that more and more. The IPO
21 could be two to three years down the road. You have
22 people who are tired of working there. And we saw a lot
23 of press before Facebook went public that sort of
24 reflects what you were saying, where really talented
25 engineers were leaving Facebook to go to Google because

1 they said why am I making you know, whatever, \$150,000
2 here with no upside on my equity for the foreseeable
3 future where I could go to Google and make 175 and have
4 publicly traded equity. Maybe my grant's not as rich,
5 but it has real value to me immediately.

6 And so that was a factor that Facebook
7 considered when it made the decision to go public, was
8 that they wanted to be a competitive employer. And
9 there's a lot of private companies that want to be
10 competitive employers but aren't ready to be public yet.

11 MR. GRAHAM: Sonia.

12 MS. LUNA: I wanted to go back to the proposed
13 section 4(a)(7). What are the top two changes from
14 what's existing now that's in this proposed section
15 4(a)(7)?

16 MS. TIERNEY: Top two changes from the House
17 passed, the financial services --

18 MS. LUNA: Whatever is in existence now that
19 you want to see in this proposed Section 4(a)(7). What
20 are the top two in your mind is different?

21 MS. TIERNEY: I don't think -- yes, there's not
22 really a top two. What was in the bill that the House
23 Financial Services Committee approved included a
24 provision that it would allow general solicitant.

25 MS. LUNA: Okay.

1 MS. TIERNEY: But Congressman Waters, who is
2 the ranking member of the House Financial Services
3 Committee and NAASA, and I believe the SEC all thought
4 that that was an unnecessary amount of flexibility. They
5 were concerned about how would I get you to tell me
6 you're accredited if I used general solicitation.
7 Because again these transactions don't have to occur
8 through a broker/dealer.

9 And so we thought that's unnecessary and we
10 agreed with them, so when we went back to speak to the
11 representatives on the Hill we said I think that's
12 something you could consider eliminating.

13 MS. LUNA: So that's one of the key changes
14 that got implemented here?

15 MS. TIERNEY: That's the key change, correct.

16 MS. LUNA: Got it.

17 MS. TIERNEY: The other thing I think is we've
18 tightened up some language to make it really clear that
19 if the company was involved in some way that it could be
20 -- what we wanted to make sure was that people who are
21 participating in these programs wouldn't be deemed to be
22 underwriters. That's a really tricky thing to write,
23 which is why I respect the staff so much when they do so
24 much rulemaking. It's really tricky to write rules that
25 create flexibility but also don't open loopholes to allow

1 bad practices.

2 MS. LUNA: So a general solicitation in this --

3 MS. TIERNEY: And just tightening up,
4 tightening up the underwriter definition.

5 MS. LUNA: Thank you.

6 MR. GRAHAM: Yes, Tim.

7 MR. REESE: I just wanted to ask some follow up
8 questions regarding the process. I'm very -- I'm
9 familiar and I understand the issue. And what I want to
10 ask is just sort of a couple rapid fire if that's all
11 right.

12 MS. TIERNEY: Sure.

13 MR. REESE: So on venture capital raise there's
14 usually a preferred return. So where is the venture
15 capital or institution involved in this and do they have
16 to give opinion? Just first question.

17 MS. TIERNEY: Do they have to give an opinion
18 in what context?

19 MR. REESE: Because they -- if I'm -- I'm a
20 venture capitalist. I usually have a preferred, which
21 means you can't sell before I get my return. So you set
22 up an exchange which somewhat causes a valuation. Is
23 that a question?

24 MS. TIERNEY: Well, again it's just a private
25 tender.

1 MR. REESE: Right.

2 MS. TIERNEY: Right. And if they have rights
3 they have to -- my company, when we did a private tender
4 we got our preferred shareholders to approve it because
5 in one case we were using our own money to do the buy
6 back and in another it was a third party, but we always
7 go shareholder approval to do the transaction. And in
8 many cases the venture capital firms are sellers in these
9 transactions. You know, they may not be selling a large
10 amount of stock but they're selling some amount of stock.

11 MR. REESE: Right. I mean, it's -- so I think
12 where I'm going is not the sort of winding road or the
13 mechanism, but I'm just saying that if I'm a venture
14 capitalist, one, you're saying that I have to --

15 MS. TIERNEY: You're a preferred holder with
16 rights.

17 MR. REESE: If I'm a preferred holder I should
18 agree.

19 MS. TIERNEY: Then you're generally getting
20 approval, yes.

21 MR. REESE: Okay. So that kind of thing, does
22 this cause a valuation?

23 MS. TIERNEY: An impact on valuation?

24 MR. REESE: Does it cause a number value of the
25 company?

1 MS. TIERNEY: Yes, I think --

2 MR. REESE: Okay.

3 MS. TIERNEY: -- in every case what we're seeing
4 is the price at which the tender is done is the price the
5 company utilizes for 4(9)(a) purposes for the rest of
6 that year.

7 MR. REESE: Right.

8 MS. TIERNEY: Absolutely.

9 MR. REESE: Right. And so in your experience
10 how -- and certain laws, are they -- is there an ideal
11 model from your end that if you're going to do this and
12 you know you're going to try to do an IPO and you don't
13 want to set the market, right, you want the market to set
14 based on the reaction, do you -- -is there a general
15 practice of where you do this so that you don't cause a
16 number versus another number --

17 MS. TIERNEY: You mean a number that would have
18 to be considered for your IPO?

19 MR. REESE: Yes.

20 MS. TIERNEY: Is that what you're -- I'm just -
21 - I'm so sorry, I'm not understanding the question.

22 MR. REESE: Yes, yes.

23 MS. TIERNEY: All right.

24 MR. REESE: So if you would do -- right, I do
25 a --

1 MS. TIERNEY: So say you do a preferred, you do
2 a third party tender in 2014 and you know you're doing an
3 IPO in 2015, then I would probably think that your tender
4 value would be considered by your underwriter in deciding
5 where to vote the book. If it's 2016 probably not.

6 MR. REESE: Right.

7 MS. TIERNEY: So I think its how concurrent in
8 time is the tender with the IPO.

9 MR. REESE: IPO.

10 MS. TIERNEY: But if you looked at the Facebook
11 IPO there was about -- I think it was less than 1 percent
12 of their shares had been traded in the secondary market
13 pre-IPO. And there was disclosure I believe, at least
14 market disclosure, that the underwriters didn't feel that
15 they needed to take into consideration the secondary
16 pricing because it was wonky, you know. Some people were
17 willing to pay anything to get into Facebook stock --

18 MR. REESE: Right.

19 MS. TIERNEY: -- not through our market because
20 we ran auctions where there was parameters of sensibility
21 I would like to call them. But in that case the
22 underwriters were not -- we don't feel like it's
23 necessary to take this small amount of secondary
24 liquidity into calculating the price that we're going to
25 go and market the offering at.

1 MR. REESE: Right. And those -- so what I'll
2 say, those are to me the extreme examples --

3 MS. TIERNEY: Correct.

4 MR. REESE: -- because those are less than 1
5 percent of 1 percent. But what I'm looking at is the
6 average company, not many of them are this size of your
7 average and them creating -- you're getting a 20 percent
8 participation by all shareholders, correct, causing a
9 value set and all of a sudden getting -- because this is
10 market, real time, you're getting an exit opportunity.
11 It doesn't have to be IPO because at auction IPO is great
12 because then the highest bid goes up. But oftentimes
13 it's going to be perhaps a set and being able to get kind
14 of cornered.

15 So I'm just -- so that's just my concern is
16 that if you don't -- if that person doesn't space it
17 right there could be that unintended consequence, and not
18 dealing with the rosy picture because the upside picture
19 is always great stories. But it's just when you do
20 unintended consequences from your actions that's the only
21 thing I'm --

22 MS. TIERNEY: I think that these are -- I mean,
23 the transactions that we're seeing they're very
24 thoughtful. The prices, if it's a third party tender the
25 price is negotiated between the company and the

1 institutional investor who is buying into the company.
2 So there's a pretty robust negotiation process going on
3 there before the price is set for the tender. And
4 because the company chooses when to launch the tender and
5 they're doing it with their law firm and their board,
6 it's I think a fairly -- it would be fairly atypical for
7 an opportunity to exist for them to do it in a manner
8 that's not part of their timeline for an IPO.

9 MR. REESE: Right.

10 MS. TIERNEY: But that's just our experience.

11 MR. REESE: No, I think new second -- my point
12 is this has nothing to do with you. Sometimes -- your
13 business -- because I think you're looking at it as I'm
14 talking about Second Market where I'm talking about the
15 market.

16 MS. TIERNEY: That's only my experience. So I
17 don't --

18 MR. REESE: Right. So I guess I'm -- we're
19 going to look at the whole thing. So my thing is from
20 the aspect of you're getting the -- you sound like you're
21 getting the crème de la crème.

22 MS. TIERNEY: Well, we tried to help place this
23 and we tried to help a much less, you know, sexy
24 contingency of private companies, which were private
25 community banks, and we just couldn't do it. I mean, we

1 spent 18 months and hundreds of thousands of dollars of
2 like legal research to try to figure out how to make that
3 work and we couldn't do it.

4 MR. REESE: Right.

5 MS. TIERNEY: And that was a real
6 disappointment to us. I mean, part of the problem was
7 that they are very, high touch shareholder bases. So
8 where maybe an employee of a tech company is 23, knows
9 how to fill something out electronically on line and has
10 access to the Internet, a lot of these bank shareholders
11 didn't have access to the Internet and didn't want to
12 fill things out on line. So we're literally sending
13 employees down to the bank to sit in the lobby and help
14 people fill out documentation. That's not an effective
15 revenue generator for a broker/dealer who is trying to
16 create a scalable model.

17 So that was part of the problem. The problem
18 was not being able to locate buy side interest. So even
19 though at that point in time we had 60 or 70,000
20 accredited investors on our website we couldn't market
21 any of these opportunities to our clients, and that just
22 made no sense. Because again if they had primary
23 opportunities we would have been able to do that.

24 MR. REESE: Right.

25 MS. TIERNEY: It was the fact that they were

1 secondaries that changed the rules.

2 MR. REESE: Well, I'm going to end but I think
3 that supports my point that the -- it's the deals
4 everyone wants that you're getting. I would want
5 Facebook, Alibaba, or the ones you -- I saw you write.
6 That's it. I love that. I would love to get that
7 employee's stock and buy it potentially at a value today
8 and get the capital appreciation when they go public.
9 But I think what we have to look at is everyone as well.

10 Thank you, Annemarie.

11 MS. TIERNEY: You're very welcome.

12 MR. REESE: Excellent company.

13 MS. TIERNEY: Thank you, thanks.

14 MR. GRAHAM: Sara did you -- you had a question
15 earlier. Okay. Milton.

16 MR. CHANG: Just to clarify, it seems like the
17 next obvious extrapolation step is that you can in fact
18 help a company raise money as well since you are already
19 have accredited investors lined up.

20 MS. TIERNEY: So that's something we used to
21 do. We used to help companies raise primary capital.
22 But our business model was really platform based, and I
23 think what we found over two or three years with
24 attempting to help companies raise capital was that you
25 really have to be a more traditional phone based

1 broker/dealer to make that effective, and people want a
2 phone call, people want to be marketed to. Just sending
3 out e-mails wasn't sufficient.

4 So we started partnering with some platforms
5 like Angel List and Circle Up and some other funding
6 platforms to provide opportunities for those investments
7 on our platform, but ultimately that wasn't a place where
8 we were making money and the business basically segued
9 away from that. We're constantly segueing away from
10 things into new things, so I don't know. But like
11 tomorrow we could be doing something completely
12 regulatory, legal, but I don't know what it is yet.

13 MR. GRAHAM: Shannon.

14 MS. GREENE: So to back up just a tad. I'm
15 trying to figure out in my brain how this is working. So
16 is really the benefit to the employees? I mean, the
17 company doesn't get anything out of this other than
18 control, whose going to get the ownership when the
19 employee sells or --

20 MS. TIERNEY: The price.

21 MS. GREENE: -- exercises the stock option, gets
22 those stock and then it sells to a third party if the
23 company didn't -- so there's no -- there's no benefit to
24 the company other than controlling, ultimately
25 controlling the ownership?

1 MS. TIERNEY: The benefit to the company is
2 making their shareholders happy, right, making --

3 MS. GREENE: Well, yes, sure.

4 MS. TIERNEY: Yes, that's the big benefit to
5 the company.

6 MS. GREENE: And controlling who the next owner
7 is --

8 MS. TIERNEY: Correct.

9 MS. GREENE: -- once -- okay.

10 MS. TIERNEY: Correct.

11 MR. SAADE: Sizing, I know you kind of alluded
12 to a 10 percent. Just trying to get a sense for the
13 sizing. 1.4 billing is admirable, but it seems low.

14 MS. TIERNEY: It's only 40 deals.

15 MR. SAADE: Right. So if you were to
16 guesstimate how big this is, right, how would you -- how
17 are you guys -- how big do you guys think the market is?
18 This is your business.

19 MS. TIERNEY: I can't quantify that. I don't
20 know. I mean, we got into private tender offers in 2012
21 by accident. We had a company who had acquired a
22 subsidiary in India and so they had a lot of shareholders
23 in India that had very, very small shareholdings. And
24 this was before the JOBS Act was enacted, and they were
25 very concerned about having to register because of the

1 500 shareholder threshold.

2 So they were the first company that hired us to
3 do a private tender and they did an all or nothing tender
4 into this employee base in India and said if you want to
5 sell you have to sell everything. And the price was I
6 think double kind of the 4(9)(a) valuation. And they
7 were able to, you know, get -- and we had to like
8 physically mail documents to India. It was not an
9 electronic solution, as we learned a lot through that.
10 But I think they were able to get about 300
11 shareholders in the subsidiary to participate, so it met
12 the company's goals, the shareholders were delighted
13 because they actually got some real money for shares in a
14 company that just acquired them, and that's sort of how
15 we started.

16 So two years ago I don't think I would have
17 been able to say that we would have closed \$1.4 billion.
18 And that's not a huge number, but that's a big number
19 from a business where maybe it was \$300,000 two years
20 ago. So I think as you see the number, the original
21 number that I put up of there's now 73 venture capital
22 backed firms with over \$1 million of capitalization in
23 private companies compared to 13 in 2012. The more that
24 number goes up the more business we're going to have
25 because those companies are very late stage, pre-IPO or

1 potentially going to stay private for however long as
2 they want to. But they're going to have a growing
3 shareholder base that wants to get some liquidity. So
4 the more that number goes up the more business is going
5 to go up.

6 MR. GRAHAM: Sonia.

7 MS. LUNA: Just one final comment. Can you
8 just give us your two minute sales pitch on your
9 concluding remarks of what you want this advisory
10 committee to address? I just wanted to get a synopsis of
11 that.

12 MS. TIERNEY: Sure. I think that as I said
13 earlier this is a change, a rule whose time has
14 definitely come. It is an absolute necessity to
15 facilitate capital formation going forward. It is an
16 absolute necessity that some rule along these lines gets
17 adopted in order for a venture capital exchange to be
18 successful, otherwise the amount of stock that could
19 trade on a venture capital exchange in a private company
20 space is very, very limited and there won't be liquidity,
21 and that will be a problem.

22 Again it mimics existing opinion practice.
23 There's nothing controversial in this rulemaking that has
24 been brought to my attention by the people we're talking
25 to on the Hill or regulators that we've spoken to. They

1 may have different views, but not that have been
2 expressed to me.

3 It will impact communities significantly if
4 people can exercise and put money back into communities.

5 It provides money to the states in a very meaningful way
6 in states where there's a big private company, you know,
7 business practice. There's no existing practice that
8 shows that there's problems in secondary trading. So the
9 SEC Small Business Advisory Forum, I always get the name
10 wrong, but they recommended this a year ago and I guess I
11 think it was recommended again this year. So it's
12 something that's been brought to the SEC's attention for
13 several years.

14 Congressional support, I just love to see the
15 committee acknowledge the importance of legislation along
16 these kind of lines or suggest the SEC actually move to
17 try to put out rulemaking on its own, which I would love
18 to see. I just -- that's it, that's my -- not a very good
19 sales pitch, but that's my pitch. I've been pitching you
20 for an hour and ten minutes, so I'm like losing steam.

21 MR. GRAHAM: Catherine.

22 MS. MOTT: Thank you, Annemarie. I read all
23 your materials and I really value the thought that you
24 put into this. So I run an Angel group and I'm the chair
25 emeritus

1 of the Inter-Capital Association, so I'm thinking about
2 how this impacts my market and what I see.

3 One is there's no doubt early stage companies
4 that are hiring people can't afford to pay market
5 salaries, so they offer these options. And I think that
6 people who put in this amount of very hard work, and
7 we're talking 80 hours a week plus, in four years, right,
8 most --

9 MS. TIERNEY: Yes, in several years.

10 MS. MOOT: -- several years. So I really like
11 the benefit of this going to those folks who are --
12 haven't been paid market salaries and have the option to
13 do that.

14 Number two is I think about how Angels behave
15 in the marketplace, and we can't help ourselves. We get
16 paid capital if we get any liquidity event. We put more
17 money in the marketplace because we're looking to build a
18 portfolio of 18, 20, 25 companies to manage risk. So the
19 other thing is I would tell you the individual Angels
20 that maybe are less sophisticated when they have to hold
21 things for so long, they give up in the market. They
22 quit deploying money in the market, so if we had a way of
23 even rewarding them and keeping them in the market and
24 keep them engaged. So those are some of the things that
25 I see that are valuable with this.

1 MS. TIERNEY: Those are really excellent
2 points, Catherine. The Angel investors point I think is
3 really important to kind of reiterate. Most Angel
4 investors if they take a position they're deemed to be
5 affiliates. So if they have more than 10 percent in the
6 private company they're deemed to be affiliates. They
7 cannot resell under 144. So the only way that they get
8 out of the position is through a 4(a)(1-1/2) transaction.

9 One of the things that we looked at when we did
10 the analysis around the legislation was the fact that
11 it's not just employee money that goes back into the
12 community, it's Angel money that goes back into the
13 community and founder money that goes back into the
14 community. My boss is an addicted entrepreneur. Like
15 give him a million dollars and he's going to start one or
16 two more companies and that's more jobs and more business
17 stimulation.

18 So that's -- most of these Angel investors I
19 think, you know, you'll know them better than I, but most
20 of these Angel investors are really not looking for quick
21 returns. They're looking for the way to really help grow
22 something impactful and long term successfully. So the
23 ability to give them the opportunity to put more money --
24 to take something out of something successful and start
25 something new I think that's really exciting.

1 MR. GRAHAM: Okay, Charles.

2 MR. BALTIC: Just one quick follow up question.

3 It sounds like you have a preference or Second Markets
4 has a preference for a Commission rulemaking solution
5 here versus a legislative solution. I just wanted to
6 make sure I understood that and what the reasons were for
7 that.

8 MS. TIERENY: So to be 100 percent clear, I
9 support whatever gets it done faster.

10 MR. BALTIC: Okay, thank you.

11 MS. TIERNEY: And in a workable fashion, right.

12 So if it's along the lines of what the Hill is currently
13 contemplating, I think it's non-controversial, investor
14 protection is baked in, and sensible, if it got put out
15 for public comment and there was this idea that there had
16 to be layered into things like cold periods or disclosure
17 or filings, it's going to kill it. So I think that the
18 staff of the SEC will do a fine job as they always do of
19 putting something out for public comment, but they have
20 no ability to control what comes back in or how the
21 Commission ultimately decides to approach something.
22 So being an SEC alumni it feels very uncomfortable
23 to me to be talking to people on the Hill and saying
24 here's a piece of legislation that you may want to use to
25 follow up -- drop sec -- 2.0. Which is I why I've tried

1 to make sure I've included staff and NAASA in all these
2 conversations, because we're not trying to railroad
3 anybody or do something that is bad for the market.
4 But we just can't -- this can't be something that
5 takes another ten years to get done. That's part of the
6 issue.

7 You know, we had -- general solicitation was a
8 recommendation to the Commission for how many years and
9 changes to the 500 shareholder number was a
10 recommendation for how many years, and you know they are
11 very busy with a lot of really important things. These
12 are not as important maybe as a lot of other things on
13 their plate. So I don't know. I would just like to see
14 it get done.

15 MR. GRAHAM: Yes.

16 MR. HIGGINS: Annemarie, one question I have is
17 the language of the statute that you've proposed places a
18 lot of emphasis as does 506 on the accredited investor,
19 right. And you posited the situation of the tender offer
20 where companies provided the relevant information, et
21 cetera. One of the things about 506 is the accredited
22 investor definition always has meant to be a proxy for
23 someone who is able to get that information from the
24 company when he or she makes the investment. That may
25 not be the same where it's a secondary seller. How do

1 you think about that in the context of, you know, you
2 talk about it as the investor protection baked in, which
3 I assume is the accredited investor?

4 MS. TIERNEY: Correct.

5 MR. HIGGINS: And I just wondered whether --

6 MS. TIENEY: And the distribution.

7 MR. HIGGINS: -- if there's a slight gap because
8 you've got a secondary seller who may or may not have the
9 information to make available to his or her seller.

10 MS. TIERNEY: So a few points. One, that's
11 exactly right. As I think we talked about a little bit
12 earlier the vast majority of these sellers will not have
13 the legal ability to provide information to buyers. They
14 just can't. If you're an employee you're not going to be
15 able to provide information to a third party buyer unless
16 the company allows you to do that. If you're -- say
17 you're a former employee or you invested six years ago in
18 a company that you don't really have a relationship
19 anymore, you certainly don't have any access to
20 information and you certainly won't be able to provide
21 that to a buyer.

22 I think the other thing that's really important
23 to keep in mind is current opinion practiced around
24 4(a)(1-1/2) does not require that opinion -- that
25 information be provided in a transaction. So with this,

1 again the goal of this is just to codify existing opinion
2 practice. If you layer in a requirement for some kind of
3 disclosure I don't know how that works. What's the
4 disclosure? And then what you end up with is there some
5 kind of a specific amount of disclosure required to be
6 provided.

7 Does it have to be provided to the states?
8 Does it have to be provided to the SEC? And then you get
9 back into kind of the proposed Reg D planet where people
10 say something becomes unworkable because these are
11 private companies. They don't want to provide
12 information publicly. If they wanted to provide
13 information publicly they would be publicly registered.

14 So we hear a lot from both sides.

15 MR. HIGGINS: Just to follow up. The analog
16 would be in 144(a) where the --

17 MS. TIERNEY: Correct.

18 MR. HIGGINS: -- exemption is premised upon the
19 purchaser having the ability to request from the issuers.

20 MS. TIERNEY: Correct. But you see big boy
21 letters in every single one of those deals, right. They
22 never have information. But they're quips so, you know,
23 they're a different level of an investor. But again I
24 think realistically the vast majority of these
25 transactions if this legislation passed are going to

1 occur through a broker/dealer, and that broker/dealer has
2 obligations to make sure the investment is suitable for
3 the buyers they locate to provide -- there's protections
4 built in.

5 It's not like I'm going to put an ad in my
6 local newspaper saying who wants to buy my Second Market
7 stock or put it on Craig's List. That's not going to
8 happen, at least I won't do that. But at the end of the
9 day the buyer is accredited, they're meant to be
10 sophisticated. You all considering changes to that
11 definition to make it easier for people to invest in 506
12 offerings, you know, I don't -- I don't know why you
13 would make it harder for secondary transactions than you
14 would for primary transactions.

15 MR. GRAHAM: Any other questions, comments?
16 Thank you, Annemarie, that was excellent.

17 MS. TIERNEY: Thank you.

18 MR. GRAHAM: I appreciate it very much. We're
19 going to be talking about venture exchanges this
20 afternoon. So let's table this discussion for now. I
21 think that everyone has been very good. Everyone has sat
22 quietly and paid attention. Now you get a break for
23 lunch. So let's adjourn until 1:45. Thank you.

24 (Whereupon, at 1:45 p.m., a luncheon recess was
25 taken.)

1 A F T E R N O O N S E S S I O N

2 MR. GRAHAM: So we will get started. This
3 afternoon, I think we will hear first from David Weild,
4 and then I think we hear from Mr. Molinari. Correct?

5 MS. JACOBS: Correct.

6 MR. GRAHAM: So, Chris, would you like to
7 introduce some people?

8 MS. JACOBS: I will. Thank you.

9 As you heard from Chair White and other
10 commissioners this morning, venture exchanges and other
11 possibilities for facilitating secondary trading for
12 private and/or smaller companies are topics of
13 significant interest to the Commission at this stage.

14 This afternoon, we are pleased to welcome two
15 distinguished speakers, who have been looking at these
16 issues for a very long time. We appreciate them coming
17 to share their expertise with us. First up will be David
18 Weild. David is founder, chairman, and CEO of IssuWorks,
19 a capital markets investment bank that focuses on public
20 equity offerings and aftermarket support for companies.
21 He is former vice chairman of NASDAQ, and he was head of
22 the capital markets group at Grant Thornton. David has
23 written a number of pieces for well-known publications
24 advocating for changes to help the IPO market for smaller
25 firms looking to go public. David was also recently

1 asked to author a study for the Organisation of Economic
2 Cooperation and Development, which was entitled "Making
3 Stock Markets Work to Support Economic Growth," and
4 presented these findings in April 2013 to the 35 member
5 nations of the OECD, the IOSCO, and the European
6 Commission, a lot of initials, David.

7 Anyhow, David was also actively involved in the
8 passage of the Jobs Act. I think this is where this
9 committee had an opportunity in prior years to meet and
10 bring David in on some different subjects.

11 Alongside David, we are pleased to have Vincent
12 Molinari. Vincent's most recent startup is Gate Global
13 Impact, a firm that provides an electronic marketplace
14 platform with market infrastructure and related services
15 for private and public investment with a sustainable
16 social and/or environmental component.

17 He is also the founder of Global Access
18 Holdings, LLC, a financial media and analytics company
19 which identified a global trend line of illiquid
20 securities and the potential market need for alternative
21 asset-trading platforms.

22 Prior to Global Access Holdings, he was
23 chairman and CEO of Burlington Capital Markets, LLC, a
24 financial services company specializing in institutional
25 execution services and investment banking activities.

1 Like Annemarie Tierney, whom you heard from
2 this morning, both David and Vince have testified before
3 Congress on issues related to capital markets and early-
4 stage companies. We are pleased to have them here this
5 afternoon and appreciate your attendance.

6 So, with that, I will turn it over to David.

7 MR. WEILD: Terrific. Thank you, Chris. And,
8 Stephen and members of the SEC, it is a delight to be
9 back. I am always kind of surprised and honored that
10 people still want to hear what I have to say.

11 I put my red, white, and blue epaulettes on
12 every time I come down here. What I really am interested
13 in is understanding how we can drive growth to this
14 economy. I think that we have done a lot of research
15 that looks at the degradation, if you will, of the small
16 cap economy and ECHO system. We think it is part of what
17 we call equity supply chains in that when you bore a hole
18 on that part of the economy, it actually creates a
19 vicious circle. It trickles all the way down to the
20 startup part of the economy.

21 I don't know if people had occasion to read
22 Robert Litan, who is the economist who published in
23 Brookings Institute in foreign affairs, but he made the
24 observation or discovered that going back in the '80s, 14
25 percent of all companies of the United States were so-

1 called startups. They were one year or less in age. And
2 now it is only down to 8 percent. We think that these
3 are actually related.

4 So what we are trying to do, you know, through
5 all of the outgrowth of our studies at IssuWorks is we
6 are just really kind of bearing down and trying to
7 understand what is wrong with the distribution model. We
8 think fundamentally because the economics dissipated,
9 that we collapsed a lot of the secondary and tertiary
10 distribution. So by that, I mean the middle market
11 institutional sales desks on Wall Street now you may have
12 1 salesman covering 100 institutional names. They are
13 taking orders. They are not presenting them. And a lot
14 of the names that we use to allocate stock to are not
15 reaching the calendar.

16 I have had this conversation with Dan Chace
17 before. I asked him I think at one of the prior
18 meetings, "Are you getting allocations in new issue
19 equities?" He should be because he is running 13 -- I
20 don't even know what the number is -- \$13 billion. It is
21 growth equity. They are long-term investors,
22 fundamentalists. They don't have access, effectively, to
23 Goldman and Morgan because there are about 60 behemoth
24 institutional investors now that are generating 90
25 percent of the commissions to the street because of this

1 hyper-efficient turnover rate. We used to probably
2 allocate to those same accounts, but the market was much
3 more forgiving because with quarter point spreads, if you
4 go back to the old NASDAQ markets, we used to resell,
5 remarket. Now there is no money in that business. So
6 the stocks are not supported. So that is what we do.

7 This is just a list you have that I am not
8 going to belabor of the papers that we wrote. We were
9 the first to effectively discover that the small IPO, the
10 bottom of it, that market fell out. And, coincident with
11 97 and 98, during the dot-com bubble, people hadn't
12 looked there. It was because we believe of the one-two
13 punch of the letter-handling rules and then something
14 called Regulation ATS, which, actually, not
15 decimalization was the first real leg down to the
16 collapse in the economic incentive. So we went from what
17 were quarter-point quoted spreads down to a 32nd or 3.125
18 cents almost overnight.

19 For me, it is not theoretical. I was running
20 businesses. I was head of strategy, strategy planning,
21 co head of strategic planning and banking research sales
22 and trading at Prudential Securities. We cut research.
23 We cut capital. We changed the stocks that we were
24 trading. We went up market as a result of some of these
25 changes. It was directly because we were losing money

1 with the smaller stocks.

2 I am going to be, I think, in Istanbul on the
3 10th of April to speak to the OECD G-20. They have been
4 socializing our work broadly. This was the original op.
5 ed. that appeared in the Wall Street Journal that
6 effectively called for a market model focused exclusively
7 on small cap stocks. It was back in 2011.

8 So I want to speak briefly about the problem,
9 why it is important, the primary cause in our view, the
10 solution, which we think is venture exchanges or small
11 cap exchanges, and then ultimately almost a call, which
12 is let's manage by objective, which is if one of the
13 things that the SEC is tasked with, which is capital
14 formation -- you know, what are the vital signs? How
15 many IPOs should we be doing? We have numbers which may
16 shock some people as being extremely high, but we will
17 show you how we get to them.

18 So the problem, then, is that the United States
19 fell from number 1 to number 12 in small IPOs defined as
20 sub \$50 million. Now, we have an extremely large
21 economy, much larger than numbers 3, 4, 5, 6, all the way
22 down to 12 on the list. So we shouldn't have dropped
23 like that. And that occurred starting in 1998. We have
24 now fallen to number two in large IPOs. This is the work
25 that came out of the OECD, which was published in 2013.

1 I don't know where it is right now but my guess is not
2 much different. The Robert Litan work that we fell from
3 14 percent of all companies were startups to 8 percent.
4 The U.S. has fallen from about 9,000 listed operating
5 companies to 5,000. We have said that you should be at
6 13,000 if you hadn't changed market structure so that
7 delta, if you will, which is about 8,000 listed
8 companies, we believe could be worth 10 million jobs to
9 the U.S. economy.

10 The U.S. IPO market, you know, in sort of round
11 numbers was in the pre-dot-com bubble era. In the five
12 years leading up to it, we were doing about 500 IPOs a
13 year. We have averaged 150-160 or so since the dot-com
14 bubble, so 2001 to present. We should be dealing 950.
15 If you GDP-weighted or you took a 3 percent GDP growth
16 rate from the early 1990s and just carried it forward and
17 we haven't changed market structure, that same 500 would
18 be worth about 900-950 today. We have heard, Stanford
19 economists have told us, that that is not a crazy thing
20 to do, GDP-weight the numbers of IPOs.

21 So what really happened was by the
22 distribution, we have seen a decline. I mentioned the
23 middle market institutional distribution decline in
24 fundamentally based retail distribution. By that, what I
25 mean is that when you can't earn a living any longer

1 marketing stocks because of the self-directed model
2 collapse, the commission incentive and the spreads
3 collapse, we have now converted into a business where
4 retail brokers are compensated based on assets under
5 management. It is not a stock-broking business or a
6 bond-broking business any longer. And, as a consequence,
7 if you will, the competition of ideas and the remarketing
8 of shares declines.

9 It is fine if you are a large cap stock, which
10 academics will say are symmetrical order book stocks,
11 they benefit from the network effect. Thousands of
12 buyers and sellers are looking at Intel and Exxon at any
13 point in time, but when you start to look down to
14 progressively smaller capitalization in stocks, they
15 start trading big buyer/no seller, big seller/no buyer.
16 And if somebody can't earn a living finding the other
17 side of that trade, then very quickly institutions start
18 pulling capital up market, and they start to abandon
19 stocks.

20 So it is acutely dysfunctional. At the low
21 end, the sub-\$100 million equity market value part of the
22 market, it is, you know, pretty dysfunctional. Under
23 250, under 500 million, it is dysfunctional.
24 Interestingly, under \$500 million in equity market value
25 and lower listed stocks, not including over-the-counter,

1 is about 50 percent of all listed companies in the United
2 States. So it cuts a big swath.

3 So a lot of people are celebrating about the
4 IPO market. What I would like to say is, "What IPO
5 market?" We have had this massive bull market here.
6 And, you know, not with a whimper but with a sigh, we
7 have if you look at 1991 on the far left and 2014 on the
8 far right, the dark blue swath is sub-\$50 million IPOs.
9 The light blue swath is larger than \$50 million IPOs.
10 And you can see that the small IPO really started a
11 precipitous decline starting in 1998 with the
12 implementation of Reg ATS. It has never recovered.
13 Interestingly, it used to be about 80 percent of all
14 IPOs.

15 So, you know, when you look at the size of that
16 bull market, the current size, we should have been
17 putting up much bigger statistics. It is an economy.
18 But we can't. The question is why.

19 This appeared in the equity capital formation
20 task force report to the U.S. Treasury. It just shows
21 you that Europe and Asia were doing better in terms of
22 adding listings. I think you are starting to see it
23 buckle in Europe right now. This is one of the reasons
24 why the European Commission is so concerned and starting
25 to look at their small cap markets. Because it is the

1 electronics markets people are starting to understand if
2 you are not careful can really pull the carpet out from
3 under small cap support. So we think we should be at
4 13,000-ish listed companies now if we hadn't changed the
5 market model. That is how we get there.

6 So this is the collapse of the investment
7 banking ECHO system. This is 1994 IPO lead managers.
8 These are all of the firms that lead managed at least one
9 sub-\$50 million IPO. And the red ones are firms that are
10 no longer around.

11 This is 2014 Bookrunners. You can see it is a
12 much smaller group. Now, a lot of the equity research is
13 deceiving. It is overstated, even though a lot of people
14 will say, "Wow, there is a lot of equity research for
15 small cap companies." In some respects, it is overstated
16 because there is no economic model to monetize it. So
17 that research isn't actively being marketed many times.
18 It just sort of sits on the shelf. It does provide a
19 service, which is that, you know, institutions will know
20 that there is some work that has been done. The model
21 can accelerate their ability to kind of do their
22 analysis. If it is an Excel spreadsheet, they will pass
23 the models around. But there is not a lot of active
24 phone calls being made because at one or two cents a
25 share, nobody can make enough to make a meal out of.

1 This was data that we pulled from the NVCA. It
2 shows the percentage of venture-funded companies that are
3 going public. You can see it just drops off a cliff.
4 Now, I shaded the gray area there because that crop or
5 that cohort, they are not mature enough to see how many
6 will actually go public yet because there is a wag
7 effect, right? It has to do with when you go to the
8 1970s, they have all benefitted from a gestation. In
9 that case, they were probably going public. Three-four
10 years was pretty standard. Today it has been closer to
11 seven or eight years, maybe a little bit better since the
12 Jobs Act came into effect and the bull market bullied,
13 and we know that we have got some better short returns.

14 By the way, testing the waters has been a real
15 boon, particularly for biotechnology, because the equity
16 capital markets people have been able to broaden sort of
17 the mafia of eight institutional investors that were
18 driving all pricing out to a broader group of, say, 45.
19 I hear this. This is anecdotal from firms like Cowen and
20 Company and Piper Jaffray.

21 Why it is important. Well, jobs, poverty.
22 Now, I don't want to come off as being overly Pollyanna,
23 but, you know, I speak to a lot of African American
24 groups that are very interested in entrepreneurship. If
25 you look at the Brookings Institute data, the African

1 American community is under a lot of pressure and a lot
2 of reasons. If you don't have full employment and you
3 don't have an education and you don't have a job, then
4 you are unemployed. There tends to be more of that in
5 the African American community, where now I think 60
6 percent of kids are born to single mothers. So if we can
7 do things that drive up unemployment as a nation, we are
8 going to start to take pressure off of some of these
9 young people. I think it behooves us to do everything we
10 can in our power, and I think this is one of the levers
11 that we can start to pull.

12 Retirement. Obviously if we can drive up our
13 economic growth rate, it is going to add to the coffers
14 to fund retirement. And, obviously, my view, the cures,
15 I have very little confidence in human ability to
16 restrain themselves, but I have a lot of confidence in
17 the ability of scientists and engineers to solve big
18 problems. As scientists and engineers, I think we
19 accelerate our ability to solve, find the cures for
20 cancer, renewable energy, ad internet security.
21 Obviously, a great or a better economy drives tax
22 revenues. Those tax revenues are important to ultimately
23 national security and a strong military. So these things
24 are absolutely critical. So I have to apologize for
25 being a touch Pollyanna.

1 Primary cause. For me, it is capacity. We saw
2 the degradation in the system, and it is with economics.

3 There is inadequate economics. It is fine to trade
4 large cap stocks with a penny. It is not fine to do that
5 for small cap, micro cap, and nano cap stocks. So a one-
6 size-fits-all market model, which naturally works for
7 liquid stocks, fails illiquid stocks. And that is the
8 crux of the matter.

9 A lot of discussion about cost to issuers. I
10 think it is kind of a secondary issue. Frankly, I think
11 you could get rid of Sarbanes-Oxley tomorrow, and you
12 would not bring back the small cap market in this
13 country. So whether we want to do scale disclosure, the
14 bigger costs, I think, are many times the transaction
15 failures, the stocks trading down, the aftermarket
16 failures. To me, a lot of the reason why entrepreneurs
17 shy away from the public equities markets when they are
18 smaller capitalization is because, number one, they can't
19 get people -- there is no ECHO system to take them
20 public, but also they are afraid of what the outcome is
21 going to be. It is not even so much the more rigorous
22 disclosure in my view.

23 This was the chart that I mentioned to you.
24 Actually, an earlier version was popularized in the House
25 Subcommittee on Capital Markets, 1991 on the left, 2014

1 on the far right. The blue swath, again, is the \$50
2 million IPO. The yellow line is what happens when you
3 take a 1991 \$50 million IPO and you adjust it for
4 inflation. And so it ends up being about an \$84 million
5 IPO today. You can see there has been a little uptick.
6 So we are up to 40 percent of IPOs on an inflation-
7 adjusted basis, but we really should be up closer to 70
8 or 80 percent to basically say that we are back.

9 So we think that venture exchange is the
10 solution. You know, what is a venture exchange? NASDAQ
11 in the '70s and the '80s was the de facto U.S. venture
12 exchange. We think that there are now problems with the
13 London AIM and the Toronto TSX venture because they are
14 for-profit exchanges. They both actually moved in a
15 direction to improve shareholder value by taking stocks
16 out of what was a market maker model to one where they
17 are using the electronic bulletin board. I met with
18 Winterflood, which was the largest AIM market maker, or
19 market maker, period, I think in equities in the U.K.
20 They pointed out that the London Stock Exchange was
21 promoting the larger AIM stocks off of the SEAC system,
22 which stands for Securities Exchange Automated Quotation.

23 It is very analogous to the old NASDAQ, National
24 Association of Securities Dealers Automated Quotation
25 system from years ago. They cream-skimmed, effectively,

1 but what that did was it took economics from the ECHO
2 system. And it was putting pressure, in turn, on the AIM
3 system.

4 By the way, I may have mentioned this. There
5 are quality and patina issues that also issuers have.
6 And so for me, I don't particularly care for the Nomad
7 system, which takes essentially review and pushes it out
8 to the broker-dealer system in the U.K. It is the
9 nominated adviser. I would much prefer that that stay
10 centralized at the Securities and Exchange Commission
11 because it is a market confidence issue, not to put more
12 work on your already stressed workload.

13 I met with Kevin Cowan a few years ago, who was
14 the head of the TSX Venture Exchange, president of TMX,
15 senior fellow over there. He had read some of our
16 earlier work, and I think that he understood that they
17 had taken the dealer market and converted it into
18 essentially an electronic order book market for the TMX
19 venture, which was, again, taking economics away from the
20 dealer system, putting pressure on the stocks, and
21 causing some of the quality or perceived quality problems
22 that they were having again.

23 So what I would recommend is let's
24 institutionalize the solution, create regulation venture
25 exchange, establish a venture exchange division at the

1 SEC. I believe in horizontally integrating the small cap
2 discipline. So I think that people with corporation
3 finance skills, trading and market skills, even
4 investment company skills, analysis, and even enforcement
5 skills need to be part of one horizontally integrated
6 team that figures out how to optimize because this is
7 ultimately a balance between interests of investors,
8 interests of the ECHO system. And until you
9 institutionalize that, I think it is very difficult to
10 end up with a proper product. It is going to end up
11 looking very different than I think large cap, but it
12 doesn't mean that there is anything wrong with large cap.

13 I think we saved investors a lot of money through
14 trading of S&P 500 securities. I think, though, that the
15 unintended consequence was the pressure that happened on
16 the small cap market. The two need to coexist.

17 I would charter member-owned exchanges for the
18 reasons I outlined. I think that the for-profit
19 shareholder system, that if you look at most of the
20 economics, 95 percent of trading is in companies that
21 have over \$2 billion in market value. Yet, 80 percent of
22 listed companies are sub-\$2 billion. So that is why I
23 draw the line at \$2 billion, largely because if you can
24 compete and pull listings from larger caps, it is going
25 to improve the quality perception of a new exchange. But

1 also it will create economics to feed the broader
2 ecology, ECHO system and then allow competition between
3 venture exchanges, between venture exchanges and other
4 exchanges for listings up to \$2 billion. Now, I know
5 that is bigger than people anticipated, but I think that
6 it gets a lot of people back into the game. This is
7 ultimately about lighting up a lot of those value
8 providers who were darkened because of the shift with a
9 loss, if you will, of the cash equities profitability.

10 I would exempt them from a whole list of rules,
11 and there you go. I think that we did just fine when we
12 took Microsoft and Intel public and we were looking at
13 30-page documents. Now, that is again a little
14 controversial, but, you know, just because you have
15 smaller disclosure on some level doesn't necessarily mean
16 that you have lower quality. The two, they don't
17 necessarily follow.

18 I think that a lot of what is in documentation,
19 I think I looked at the Facebook. The deal was like
20 nearly 300 pages longer. A lot of it, it is almost
21 necessarily so complicated that you have to be an
22 institutional investor to be able to wade through it. I
23 don't think consumers have a real shot at wading through
24 documentation that is that thick, so something to
25 consider.

1 I would say yes to SEC review, not state, not
2 Nomad. I would say yes to SEC scale disclosure. I would
3 say that the JOBS Act research rules should be extended
4 to all public-listed companies in this sector. I would
5 say no to exchange-traded funds and index funds. Again,
6 this is a little bit out of left field, but, you know,
7 every exchange-traded fund and index fund, you know,
8 almost every one, has one thing in common. They don't
9 buy new issues, which means that that capital, the bigger
10 they become, the more they deprive our corporations of
11 access to capital. It skims capital from the economy,
12 right? So maybe they should be required to have standing
13 orders on new issues, but I also think that they zap
14 liquidity from the system. And if you look at the
15 market-weighted ETFs, you will find that they tend to
16 drop off the smaller companies because they make a
17 decision about they don't effect the index particularly
18 well. So, again, it deprives the system of capital.

19 I am not sure that I wouldn't just prohibit
20 them from venture exchange stocks and make it solely the
21 province of fundamental managers and fundamental
22 investors. I also think culturally we diminish our
23 entrepreneurial IQ as a nation when we are buying box
24 kits and themes and we don't have to talk about
25 individual stock selection and valuations, which I think

1 is actually a very healthy educational aspect of the
2 single stock fundamental business. You are never going
3 to be able to compete single stock selection because it
4 costs more. You need people to do that with the
5 computer-based ETF and index fund business, just by
6 definition. They depress liquidity, siphon capital, and
7 undermine our entrepreneurial IQ.

8 So, in addition, some improvements to private
9 markets. You know, this is now a little bit different
10 non sequitur, but just in the private market, it would be
11 nice to see some basic disclosure, even if it is just an
12 annual audit, you know, put into the market, because I
13 think that, you know, if you are a big, visible, hot, you
14 know, social networking stock that everybody knows, you
15 don't have to give up any information because people just
16 want to buy it and they run into it blindly and that if
17 you are a very complicated technology company that may
18 have the cure to cancer because you need more marketing
19 support, you get forced into having to disclose
20 information. And so at least some standard would be
21 helpful.

22 Require consolidated tape. I mean, where are
23 the prints going? I think that would be a great public
24 service. Don't deem it to be a solicitation. Just make
25 it available so people can understand where trades are

1 actually occurring.

2 Then, finally, allow a national aftermarket
3 solicitation because of accredited investors and
4 institutions would preempt blue sky. Right now under the
5 JOBS Act with 506(c), I think you can do the primary
6 placement pretty handily, but then at some point, if you
7 need to solicit things in the aftermarket, it is not
8 clear that you don't have to file with state blue sky
9 authorities. I think that that creates a level of
10 inertia.

11 How do I go back? Can I go back on this?
12 There you go.

13 So, you know, it is a classic management
14 objective. Go, team U.S.A. What is our objective? We
15 want to be number one. We want to be number one in small
16 IPOs. We want to be number one in large IPOs. You know,
17 we want to get back up there, get our mojo working and
18 being kept on startups. You know, what are we doing?
19 You know, come together. Let's figure out what we can do
20 to reverse these trends. We want to drive up the number
21 listed, companies again.

22 Transparency. I met with one of the old heads
23 of the Division of Enforcement. You know, he was telling
24 me at the time being at the SEC when it was really
25 important for transparency as a public policy matter to

1 get companies to be public. They didn't want the
2 opaqueness of the private market. Yet, what we have done
3 now is we have actually in some instances made it more
4 attractive to stay private. So it is sort of interesting
5 how things have turned and then ultimately, you know, to
6 get ourselves back up to 500 and then 950 IPOs, whatever
7 the number is, and to see it grow at GDP rates
8 constantly. I think if we do all of those things, yes,
9 there would be a lot of failures. Yes, people will lose
10 money, but the cure has been worse than the disease. We
11 have stifled the economy, and we have stifled innovation.
12 And I think that, you know, the legacy that we want to
13 leave for our kids and our grandkids is one where there
14 is a shot at the American dream and that by virtue of
15 your hard work and perspiration, you can get out there
16 and you can give something a shot and grab that brass
17 ring of being a public company, which is, you know, how
18 entrepreneurs used to work at public markets and I fear
19 don't any longer.

20 Thank you.

21 MS. JACOBS: Thank you, David. Very
22 insightful. And I always appreciate the numbers and the
23 data. So thank you very much.

24 Before we go on, before we go on to Vince,
25 though, I would like to ask Keith. We have folks here

1 from trading and markets today that you would like to
2 introduce.

3 MR. HIGGINS: David Shillman is with us. David
4 is an associate director in the Division of Trading in
5 Markets.

6 MS. JACOBS: Welcome. You probably can't wait
7 to hear what we say, then, right? Always a surprise.
8 And, with that, I will turn it over to Vince. Thank you.

9 MR. MOLINARI: Good afternoon. Thank you,
10 Chair. Thank you to the Commission and certainly to the
11 committee. Thank you to David. I have to say publicly
12 David has been a great inspiration on our thought process
13 and the data and information going back to 2008-2009,
14 when we looked at the facilitation of capital, to the
15 private sector to small emerging companies, which are our
16 engines of growth. Forget for a moment decimalization,
17 Sarbanes-Oxley, or the handling rules, the whole gamut.
18 The fact is as a nation, we need to continue to foster
19 that capital for growth. And that is where our economic
20 recovery comes in, dare I say one of these days real
21 prosperity again.

22 Another great influence -- and I just throw it
23 out -- if anybody hasn't read "The Coming Jobs War" by
24 Jim Clifton, the chairman of Gallup, it speaks to exactly
25 I think what we are all talking about here. The biggest

1 threat to the United States of America is our lack of job
2 creation and the things that happen post that. So I just
3 throw that out.

4 David's body of work has really influenced when
5 we think about what we would say is new market
6 infrastructure. I think we have to challenge ourselves
7 in the thought process here a bit to think a little bit
8 differently.

9 One of the things with the JOBS Act in the
10 advent of the adoption of that is we are entering a
11 paradigm shift where social media, Web 3.0, is
12 intersecting with financial services in a real way for
13 the first time.

14 I think some of the challenges during the
15 rulemaking period have been how do you integrate these
16 new methods. While although we can preempt certain
17 portions of securities law, folks who haven't been in the
18 business, who maybe have historically been technologists
19 who are really good on the front-end user interface,
20 customer acquisition side don't realize that there is
21 this whole body of work on the '33 or '34 Act.

22 The other side of it is we have great financial
23 services firms who are kind of stuck in a legacy
24 mentality and don't really understand yet how do we
25 integrate, how do we embrace things like general

1 solicitation, which I think is just amazing. We will
2 talk more about that. When you combine general
3 solicitation with the changes to 12(G), you have really
4 created a new mechanism for private companies to stay
5 private longer or, frankly, to stay private forever and
6 not go public. In that period of time, they are
7 accessing capital on a primary basis, but also what we
8 need to do is create the orderly structure for secondary
9 liquidity for unregistered securities.

10 I know Annemarie touched on it earlier, David
11 touched on it. The interplay with the coexistence of
12 secondary liquidity drives primary issuances to capture
13 capital. People are much more likely. What do we all
14 ask? What is the exit before we enter the door? If we
15 can define that in a structured way around new market
16 infrastructure, I think we can continue to accelerate the
17 movement of capital in a structured way.

18 I think when we look at the fact that we now
19 have north of a trillion dollars annually in unregistered
20 securities being done, I think that is a bellwether sign.

21 As we implement more of general solicitation under
22 506(c), I think we are going to see those numbers
23 continue to grow. I think what we are seeing across the
24 board, and whether this is at the state level or the
25 federal level, is a bit of an inverted liquidity funnel.

1 We have this growth of offerings for unregistered or
2 private securities, and there is no exit.

3 We think it is paramount to speak about
4 secondary liquidity as a cornerstone of investor
5 protection. That is part of the capital formation
6 process when we look at not just capital raising but
7 capital formation being defined as having information
8 data and true investor protection around the education
9 component, and that leads to the secondary liquidity.

10 You know what? I hope you don't mind. I am
11 just going to forget about the PowerPoint slides. We are
12 just going to have a bit of a chat through it.

13 So I think we have taken the approach that
14 these really should be issuer solutions. You know, as we
15 started -- and Annemarie was great talking about the
16 early days of how Second Market had evolved as an
17 employee liquidity model. I was fortunate to testify in
18 Congress next to Barry and did a phenomenal job. But I
19 think what we have learned over the past few years is
20 that it is not just about the employee liquidity. It is
21 about the issuer. So we have to embrace the issuer and
22 have the issuer on side. That is where I think we can
23 get into all of the things that we talk about about
24 permissioning and the need for right of first refusal and
25 others. So if the issuer is on side who is looking to

1 raise capital, you then have the ability to ask for
2 information.

3 Again, I think we have learned more over the
4 past two or three years of issuers who are saying, "I am
5 not giving you any information as a private company
6 because I don't want my competitors to know." But when
7 they see the ability that they can access capital if they
8 start to put information forward, the likelihood of
9 raising capital becomes much greater. So we are seeing
10 an opening of that.

11 I think when we begin to look at solution sets,
12 we have always looked at the broker-dealer model. The
13 broker-dealer model is an existing framework we all have
14 if we take it up a level when we have broker-dealers here
15 and we have our exchanges here and we have this big
16 middle that is wide open. We have lost our distribution,
17 as David would say. I am not so sure we are going to get
18 all of that distribution back, whether we go back to
19 spreads or other mechanisms. I think we have to look at
20 the new world, the paradigm shift. The way millennials
21 are going to be investing is different than we did just 5
22 and 10 years ago.

23 So I think when we look at incorporating social
24 media and Web 3.0 as our distribution model, we are now
25 reaching out and accessing investors in a new way, in a

1 very efficient way, to close that big gap. So I think
2 when we then look at the ATS, Reg ATS, model, wonderful
3 model -- and I know David's views on hurting perhaps some
4 of our public markets, but I think there is a wonderful
5 window to amend Reg ATS to facilitate the secondary
6 trading of unregistered securities in an orderly way.

7 In the Commission's adopting release back in
8 1998, it recognized that as good as Reg ATS is for the
9 liquid markets, it hasn't completed its work on the
10 unregistered side of the market. So I think it is time
11 to go back to that. Let's fix that. That is something
12 readily available to us.

13 I will just point out a little piece of
14 history. With that adopting release, what it really did
15 say is, "ECNs, crossing engines, you have a choice. You
16 either become an exchange or you become a broker-dealer
17 that hosts an ATS. That was the decision tree."

18 Well, I think if we look at the phenomenon that
19 happened, something called Archipelago that was public on
20 the Pacific Stock Exchange did a reverse merger with the
21 New York Stock Exchange. The New York Stock Exchange
22 became public through that mechanism and still uses the
23 technology today of ARCA that was born out of this
24 crossing engine ATS process.

25 I think if you look at our other exchange in

1 NASDAQ, kind of a repeat performance. Island and Insonet
2 became NASDAQ. So I think what we have forgotten about
3 in the process is how do we incubate that next level of,
4 dare I say, exchanges? The technology is here. We have
5 the ability to dematerialize a hold of record, private
6 companies, and unregistered securities with transfer
7 agents that are governed by the SEC. That certifies the
8 books and records; gets a communication tool; but, most
9 importantly, allows a readily available mechanism for
10 that dematerialized security to move to a second platform
11 to liquidity.

12 So I think if we start to connect the dots
13 around some of the regulation, this speaks directly to
14 the venture exchange. I think these ATSEs with direction
15 and guidance from the SEC can grow up to be the next
16 venture exchanges, could be the pilot program to
17 demonstrate what could happen. The market, let's not
18 pick winners and losers. Let the market determine for us
19 what is working and what we can effectively move to
20 action.

21 We spoke about the urgency of this need. We
22 have something readily available to us today by -- I
23 don't want to say simply, but I will say simply modifying
24 Reg ATS for unregistered securities to give it
25 clarification and ease that process. In some cases, for

1 a broker-dealer to become an ATS, it is a 12-month
2 process. Let's streamline that.

3 Also, our friends over at NASA, we touched on
4 some of these conversations, but I think the ATS
5 mechanism, being that it is born out of the broker-
6 dealer, can be an intrastate solution applied to various
7 issues that the states may be looking at.

8 So I know there are tons of things that we can
9 talk about around the secondary marketplace, but I think
10 when you add information to the process, when you have
11 some level of standardization of disclosure, when you can
12 have straight-through processing on escrow, the
13 equivalent of clearing and settlement with a transfer
14 agent, yes, we are blurring the lines of public and
15 private, but we are already doing that. So let's enable
16 things.

17 Again, I will agree fully, Annemarie, over
18 there with all of your great work, 4(1-1/2). Absolutely.
19 We need to be able to generally solicit. You can't have
20 506(c) and the ability to generally solicit and then, all
21 of a sudden, 4(1-1/2), no general solicitation. We are
22 defeating what we have accomplished and certainly not
23 enabling it.

24 I think we should consider that general
25 soliciting of 144(a) should be available to accredited

1 investors, not just QIBs. We have a body of information
2 and data that is born out of a public company.
3 Availability of FA? I think an accredited investor can
4 certainly fend for himself or herself. I won't get into
5 your trap, Commissioner. I think when we look at those
6 mechanisms, that we have the solution set here and that
7 accredited investor, as we talk about revising what an
8 accredited investor is, we have a wealth of readily
9 available investors who will invest, who have the
10 wherewithal, who can fend for themselves. And I see no
11 reason why they could not be participants in a 144(a)
12 secondary purchase of securities.

13 I am trying to be cognizant of my time there.
14 I have got a minute and a half left. So I will throw a
15 little piece on there. I think we can consider with an
16 exemption that a structured ATS mechanism for
17 unregistered securities could facilitate Reg A+ offerings
18 as a primary. We have the mechanism in place.

19 ATS in an exchange is very similar in their
20 modeling. We could look at the language. It is
21 identical except the ATS is not a self-regulatory
22 organization. They can discipline their participants,
23 but they are not setting their SRO. The broker-dealer is
24 already governed by FINRA. So I think we have something
25 that we can consider as a mechanism to facilitate that

1 movement aside from the pure exchange model of Reg A+.

2 I think I have made it with ten seconds to
3 spare.

4 MR. GRAHAM: All right. Thank you, David.
5 Thank you, Vince.

6 I will open it up for questions, comments.
7 Sara?

8 MS. HANKS: Okay. I just wonder if we could
9 address what I am seeing as maybe a bit of a tension from
10 the discussion we had this morning, where we heard from
11 Annemarie that there are some companies who want to keep
12 trading close and don't really want to have wild trading
13 out of their control and encouraging people to go list on
14 venture exchanges, where I think trading would be out of
15 the control of those companies. Do you see the same
16 tension or is there a solution to that?

17 MR. MOLINARI: If that is for me, Sara

18 MS. HANKS: Both of you.

19 MR. MOLINARI: Gladly. I think this is why we
20 call it an issuer solution. So that issuer can
21 determine, they can permission what they want their
22 protocol to be. Do they want it to be an entirely closed
23 network for their own use? Sure, you can do that. If
24 they want to open it up to a broader ability, you have
25 the broker-dealer and the ATS network to extend that.

1 They could even permission levels. So they may only want
2 QIBs. If they only want QIBs, then you have a different
3 level of filtering if it is other than going deeper to
4 accrediteds. So the technology certainly exists. And I
5 think it is really the framing of the issuer that drives
6 that.

7 MR. WEILD: I think that they should have
8 choice in private markets. I mean, I have run into
9 plenty of companies that want to control who ends up on
10 their shareholder register. I think that you can have a
11 range of options like that in the private markets. I am
12 not too concerned in the public markets, in the public
13 venture exchange now or the old NASDAQ, and I think that
14 that bottle would clearly break down. I think that the
15 whole idea is to create liquidity and have
16 standardization and that ultimately if it works in the
17 public markets, that is the reason why you aspire to take
18 the company into the public markets because there is a
19 real benefit to being public. And it used to be. And I
20 think if we can get back to that place, I think we will
21 all benefit.

22 MR. GRAHAM: You know, David, this committee
23 has been interested in the venture exchange idea for some
24 time. I think we issued a recommendation essentially to
25 that effect, probably about a year or two ago. You know,

1 I, for one, am kind of attracted to the whole idea of
2 developing these other markets, these other exchanges.
3 They are there geared again for the smaller public
4 company. And we have the idea of the exchanges with the
5 five-way companies as well.

6 In your view -- you and others like you are the
7 experts. You really understand it deeply. I understand
8 that it is not -- well, we are dealing with a complex set
9 of issues. But, you know, help me a little bit with some
10 of the practical aspects in terms of what, you know,
11 maybe this committee could do to encourage movement in
12 that direction. You know, for example, you know, I think
13 we have all read your most recent article that I guess
14 comes out today. You talk about the need to kind of
15 reestablish the framework for these kinds of markets.
16 Certainly an important part of that is coming up with the
17 member exchange concept, which goes back to kind of the
18 old NASDAQ, if you will.

19 How does that happen? I mean, is there a bunch
20 of members out there just waiting for something to join
21 so that they can suddenly have a member-owned exchange
22 with this

23 MR. WEILD: Yes. I mean, it is going to
24 happen. If you have the right enablement from a
25 regulatory or legislative standpoint, it will happen

1 quicker than you might think because there is a great
2 tradition on Wall Street, what I like to call consortium
3 investments. Actually, with the bulge bracket, the major
4 firms, there are at least ten firms out there I am aware
5 of that actually have strategic investment portfolios
6 that they actively solicit and do things together.

7 So the markets.com, for instance, which was a
8 research-shared utility, is an example of one. Many of
9 the ECNs, electronic communications networks; ATSEs were
10 set up originally, going back into the '90s, as around
11 through multiple investments by multiple broker-dealers.

12 And so I think you would be surprised. I think, you
13 know, part of it is the governance. You know, you want
14 to make sure that the small firms can participate and in
15 some respects, the bigger firms make bigger use. So you
16 wouldn't have to tax them from a capital standpoint.

17 We used to play around with the governance in
18 terms of tiering. I think that FINRA does the same thing
19 right now where you have representation by smaller
20 broker-dealers. So there has to be some thought given to
21 that so that you are inclusive, not exclusive, on
22 something. I think that firms would get behind and as
23 more firms came into the business and were attracted by
24 the economic opportunity, I think you would see that a
25 robust membership occurs. It is all about incentives.

1 So there is a fellow who is on the board of
2 directors of Tuesday's Children with me. That is a 9/11
3 charity that I have been serving on for 13 years. He is
4 one of the senior guys at Goldman Sachs in charge of
5 their strategic investment portfolio. They actively look
6 for things to invest their money in that are going to be
7 supportive of their business and to take a minority stake
8 in them. So it is part of the Wall Street culture, at
9 least, with the larger firms.

10 MS. JACOBS: David, I have got a quick question
11 or a need for clarification. When you were making
12 reference to for-profit venture exchanges versus not-for-
13 profit and then you talked about it being an SEC
14 initiative, could you clarify for me? Were the for-
15 profits

16 MR. WEILD: It was for-profit shareholder-based
17 markets that concerned me because, you know, it is a
18 question of whose economics are you really essentially
19 trying to optimize? And when you are a shareholder,
20 publicly traded shareholder, based company, which is
21 NASDAQ now, New York Stock Exchange, even OTC markets,
22 you know, your mission, really, is to create shareholder
23 value. If that means that you can drive earnings by
24 collapsing, by doing something that improves your
25 economics to the detriment of the ECHO system, you are

1 going to do that.

2 That is exactly what we saw with the AIM
3 market. That is exactly what we saw with the TSX venture
4 market. You know, the TSX venture market used to be a
5 dealer market. Now it is on the central limit order
6 book. If you look at the end market -- you know, when I
7 met with Marcus Stuttard, this was what Winterflood had
8 told him, largest market maker in the London markets.
9 They took SEAC dealer, you know, traded stocks that had
10 heavy incentives for the economics of the more liquid
11 ones. They are still called AIM stocks unlisted
12 securities, but they put them into the electronic order
13 book because it was more profitable for the exchange.

14 Now, they probably won't come out and say that
15 publicly. We tried to get the information on it. They
16 were very helpful. They wanted us to write something
17 about it. And then they stopped communicating with us
18 once we were hearing that from the market. They wouldn't
19 follow up with us. But that's what we think happened.

20 It is human nature. Your job is, what is your
21 mission? If your mission is to serve the needs of your
22 shareholders, then you are going to pursue things that
23 drive your earnings per share. The two don't necessarily
24 coexist very well: the need for the ECHO system and the
25 need to drive shareholder value.

1 So if the ECHO system is, effectively, your
2 shareholders, then, by definition, you are likely to do a
3 better job of nurturing the needed economics by the ECHO
4 system to provide research capital commitment to make
5 markets, sales marketing.

6 Does that make sense?

7 MS. JACOBS: Sort of.

8 MR. WEILD: Sort of. They post something on
9 the electronic board. The dealers can't make any money
10 from it any longer because they aren't market making.

11 MS. JACOBS: Right.

12 MR. WEILD: Okay? All of a sudden, they are
13 making, the exchange itself is making, money by hosting
14 that facility. So every trade that goes off, they make a
15 little bit more money. So it is more profitable for them
16 to take the more liquid stocks and stick them in their
17 hosting mechanism. You know, it was pure economics that
18 drove them in that direction.

19 That is one of the reasons why we think we have
20 seen the end market deteriorate a little bit over time.
21 It hasn't performed as well as it might have.

22 MR. GRAHAM: Catherine?

23 MS. MOTT: Thank you, both. When I look at
24 data and I read these things, I think about how it
25 impacts behavior in the market I am in, which is angel

1 investors. Also, I am a managing partner of a venture
2 fund. So I am always for more liquidity opportunities
3 because that deploys more money into the market. So when
4 people are rewarded with returns, they end up putting
5 that back into the market. So I see real value in that.

6 The data in my portfolio matches what you are
7 talking about here. Holding periods are getting longer
8 and longer. Recently there was an article about the new
9 venture model. It is 14 years, instead of 10 years. As
10 an angel investor, we used to say five years was the
11 average holding period, and you would need twice as much
12 twice as long. We are now saying three times as much and
13 three times as long because we are holding things longer.

14 It is discouraging people in the marketplace. They are
15 less inclined to put more money back into the market to
16 create new companies and create new jobs.

17 The other thing is smaller venture funds are
18 finding it difficult to because they don't have these
19 larger liquidity options rely on M&A. So they don't have
20 the big returns and can't detract the institutional
21 investors. So the only ones that are the institutional
22 investors are the Kleiner Perkins, the Sequoias, the top
23 tier. There is no Chace for a small fund to be a top-
24 tier fund when you have to rely on solely M&A.

25 The other thing that concerns me about solely

1 relying on M&A is that many companies -- I know this from
2 my own portfolio, not many, but there is a segment of
3 companies that are acquired not to create more jobs but
4 to come off the market.

5 I mentioned to this group a couple of years ago
6 about a company in my hometown of Pittsburgh that is
7 venture-capital funded and angel-funded. It is called
8 Renal Solutions. It had an at-home device for dialysis.

9 It got acquired by Fresenius and put on the shelf
10 because they don't want it to disrupt their marketplace.

11 It was generating revenue. Had that company been able
12 to continue to maybe go public, it could have created a
13 lot of jobs, maybe disrupted the market in some places.
14 You know, it could have had a different impact on the
15 economy.

16 So I am very much supportive of this. And, you
17 know, I would love for this group to continue to have
18 this discussion and take a real close look at this and be
19 supportive.

20 MR. GRAHAM: DJ?

21 MR. PAUL: Vince, I want to kind of drill down
22 into like the practicalities of what you might be
23 suggesting so that the committee can perhaps make a
24 specific recommendation. I think it might be helpful for
25 some of us if you could walk, you know, as a BD

1 practitioner us through the process of how BD becomes,
2 obviously briefly, right, an ATS, what the pitfalls are
3 now in becoming that process and then what you would
4 recommend if we were to move in the direction of that
5 kind of solution for secondary market support, what would
6 be necessary from a regulatory modifications standpoint,
7 whether that is here, meaning at the SEC, or at FINRA.

8 MR. MOLINARI: Sure. I think we are going to
9 take the baseline that you are already a broker-dealer.
10 So let's skip the broker-dealer approval process. Call
11 it six months or a little bit either side of that. So
12 the ATS if we go back to 1998 was designed, in effect,
13 for liquid securities. We have never gone back to really
14 address what we long recognize is the fact that it has
15 not really been refined or allocated for unregistered
16 securities. So that one I think is the recognition and I
17 think an action item of the committee to fix what we
18 started -- my math isn't that good but 20 years ago
19 maybe, 17-18 years ago -- and recognizing let's fix that
20 first.

21 I think in recognizing that needs a fix, which
22 is a streamlining, working with FINRA to streamlining the
23 process, the process of becoming an ATS is rather
24 cumbersome and very long. It could be as long as 12
25 months or greater. And within that, you are really

1 applying for your ATS on a specific asset class. So you
2 could have an ATS for 144(a). It doesn't give you the
3 ability cross over a greater stack of components.

4 So I think you need clearer delineation via the
5 SEC to FINRA on the unregistered use, unregistered
6 security use, of the ATS and perhaps widening that
7 approval set that it could be for more than one category,
8 a greater stack, so you are not going back each time to
9 go through the ATS approval for another asset class.

10 So I think those are the two biggest pieces:
11 fixing what we started in '98 and giving a clearer
12 definition of how you can use multiple asset classes on
13 that ATS.

14 MR. GRAHAM: Yes?

15 MR. PAUL: David, very broadly, right, because
16 there is a lot of specificity with your awesome data, if
17 the Reg D market is over a trillion dollars, which is to
18 some extent good or bad, it is stepped into the position
19 of where the IPO markets have gone down, and that market
20 has blossomed. If the goal ultimately, leaving aside,
21 you know, some of the mechanisms by which it would
22 happen, if the ultimate goal is

23 MR. WEILD: By the way, David, I don't believe
24 that.

25 MR. PAUL: You don't believe it?

1 MR. WEILD: I think that the data on the Reg D
2 if you go back historically is incomplete. If you look
3 at what people had to file, a lot of times, you know,
4 they don't have to file what they actually raised. So
5 you don't know.

6 We sense that there is a big growth in Reg D
7 placements, but a lot of it is later-stage. By the way,
8 Catherine, everything that you said I 100 percent agree
9 with. I see the same stuff. I would argue that it is
10 even worse for early-stage venture capitalists because
11 they don't have enough money or angels. What happens is
12 they end up getting crammed down or the winners, they
13 can't keep up. So their returns drag as a result.

14 So what we have done because the funds have
15 gotten bigger and bigger is we have actually started to -
16 - I know people don't like this analogy, but it is an
17 unleashing of flesh-eating bacteria on the bottom of the
18 market. So until we get a little bit better balance in
19 there, I think it is going to be harder for smaller,
20 earlier-stage risk-takers need to have public access.
21 Until those come back, we are going to see lots of
22 examples of that dysfunction. There is no good Reg D
23 data out there as far as I am aware that really tells you
24 what has really happened to the Reg D. It is a bit of a
25 I would call urban legend that it is replacing investment

1 activity. It clearly isn't.

2 Some of the venture guys will also say that
3 there are whole swaths of the market, mom and pop, you
4 know, bootstrap companies, that need to get public that
5 are never venture-funded. They can't get to the market
6 either.

7 MR. PAUL: So, leaving aside the question of
8 whether or not the data that the SEC published in July of
9 2013 and then refreshed I think in November or at least
10 made public in November at the small business forum is
11 accurate or if it is inflated or otherwise, the goal is
12 to get more capital formation in this middle market area.

13 The goal is to have the possibility for secondary
14 trading and exit, not necessarily a public exit but an
15 exit. Right? The goal is for people to be able to go to
16 the next level. So why isn't a possible interpretation
17 of the data that you put forth an argument for some of
18 the other things that we have discussed here: loosening
19 up Reg D? By that, I mean to say expanding the
20 definition of accredited investor, which would reach down
21 into the ability of other people to participate in the
22 market. Why isn't it an argument for Reg A+, which would
23 hit this middle market, you know, pretty well inasmuch as
24 it would go up to, you know, \$50 million, which I
25 noticed, you know, that cutoff point used in some of your

1 data points? Why wouldn't those things be an equally
2 viable and perhaps less regulatorily cumbersome solution
3 than, you know, creating an entirely new market or an
4 entirely new infrastructure, which is to say a new type
5 of exchange? Can't we get at this through the existing
6 structure that we have?

7 MR. WEILD: Well, I think the reason why we are
8 talking about a holistic solution is because, you know,
9 from stumping up on the Hill and coming here, we have
10 been talking about piecemeal solutions. And I think that
11 people are starting to realize that we really need a
12 comprehensive look. And it has to work soup to nuts. I
13 think Reg A is really more disclosure. It doesn't help
14 you with the aftermarket.

15 I testified in support of Reg A. By the way, I
16 think all of the above. We need to do something. We are
17 desperate.

18 So if you look at "A Wakeup Call for America,"
19 which is a paper that we wrote where the repeal of the
20 prohibition against general solicitation came from page
21 30, it was a recommendation we made.

22 You find that all of these things are helpful
23 on the margin, but you really want to make a private
24 market robust. You want to make a public market robust.
25 We deserve to have both. So let's look at it

1 systematically and comprehensively. Let's just make them
2 both work, and I think America will be back in business.

3 I mean, I hate to say it. It is not rocket
4 science. We have taken a piecemeal approach to this
5 stuff for a long time and just getting it to work. We
6 know models that actually can work do work. We just need
7 to get it done.

8 My view is that this was the reason why I think
9 I have been asked by people in the Senate, you know,
10 "What are the things that you would focus on?" And I
11 think you have got to institutionalize the core
12 competency, you know, which goes right straight through
13 every division of the SEC around small markets. If you
14 do that and you have the real discipline around it, you
15 will have much better results, you know.

16 When I look at the committees, you know -- and,
17 as you read in my article, I see large cap buyers
18 everywhere we look. I look at investor advisory
19 committee. We have got a lot of large quantitative
20 interest out there that wouldn't know a small cap stock
21 if it bit them in the derriere. I look at the Dan
22 Chaces, for instance, the Wasatch Advisors of the world,
23 or the T. Rowes, the long-running mutual funds. There is
24 very little representation like that on the committee.
25 You know, we looked at the recent market structure

1 committee. None of the middle market investment banks
2 are represented that actually service these companies,
3 you know, day in and day out.

4 So I understand it is difficult to put these
5 committees together. There is a lot of politics involved
6 with it. But if I go to the SEC -- and I may be wrong
7 about this -- the only area of the SEC that I am aware of
8 that has a committed small cap effort is the Division of
9 Corporation Finance. If not a unique division, I would
10 love to see one in Trading in Markets. I would love to
11 see one in the investment company area and enforcement
12 because I think the needs of these ECHO systems are very
13 different and the way the stocks trade in my experience
14 are completely different. It is an old cliché on Wall
15 Street that it is a lot easier to do a big deal than it
16 is to do a small deal.

17 MR. PAUL: I have a follow-up, but go ahead. I
18 will

19 MR. GRAHAM: Dan?

20 MR. CHACE: I was just curious. How do you
21 think about the issue of adverse selection in a venture
22 exchange, which I think has been an issue for the AIM and
23 the TSX, at least in terms of your perception? I mean,
24 how do you attract quality companies as well to those
25 markets?

1 MR. WEILD: Well, that is one of the reasons
2 why we took the cap up to 2 billion, because you are
3 going to get better companies. People will look at it.
4 It gives you greater economics to the market. I think
5 there is a limit. You know, everybody I am sure read
6 Arthur Levitt, you know, op. ed. The American Stock
7 Exchange. I hate to say it, but it got squeezed between
8 NASDAQ and the New York Stock Exchange. It was the
9 listing cesspool. I think that, you know, if you create,
10 again, that horizontally integrated, you know, market
11 structure, there are a lot of good quality old NASDAQ
12 companies that can't get public today because of this
13 market structure. So I think there needs to be some
14 vigilance, there needs to be some thought. I think the
15 broker-dealer community doesn't want to have that happen
16 either. So it is going to be either reengineered around
17 listing standards, but we allowed a NASDAQ listing to
18 lots of companies that had no earnings whatever. That is
19 called the biotechnology industry, right?

20 So smaller companies are going to go out of
21 business at higher rates. They always do. But, you
22 know, I like to say look back to 1971, a small million-
23 dollar IPO of a company that missed delivery on its first
24 new product. The stock got cut, you know, by 60 percent
25 in price. So it was trading with about a \$3 million

1 float. Then they turned it around. Guys got on the
2 phone because they could earn a commission, drove it up.
3 That company is the Intel Corporation.

4 MR. CHACE: Can I ask one other question?

5 MR. GRAHAM: Sure.

6 MR. CHACE: Sorry. From an issuer
7 perspective, what do you think the financial disclosure
8 expectations would be? I mean, what would be acceptable
9 to an average issuer?

10 MR. WEILD: Oh, God. You know, I think when
11 you are looking at teeny, teeny, tiny companies, you
12 know, you want less. You know, the risk gets bigger.
13 You know, obviously there is a systemic risk of failure
14 of large companies. You need to be really vigilant
15 because one Apple blowing up at \$750 billion really
16 wreaks havoc. This is why we ended up with Sarbanes-
17 Oxley, through Enron's explosion, Adelphi, WorldCom,
18 Tyco, but the smaller companies present less systematic
19 risk. So I think that the answer probably should be
20 different for a \$10 million equity market value company
21 than a \$100 million than a \$250 million.

22 I mean, at some point, -- maybe it is at \$100
23 million -- you know, having pretty standard full-blown
24 disclosure, you know, I think is required. They have the
25 wherewithal, the economic wherewithal, to do it. Again,

1 it is an optimization problem.

2 In some respects, I think, you know, pulling
3 together disparate interests, the actual ECHO system, of
4 people that are going to invest in a \$10 million or \$100
5 million company, they would probably come up with a much
6 more informed answer than I would. So, really, for me,
7 the answer is let's get the governance right of venture
8 exchanges and how we approach these things. You
9 typically would have an institutional advisory committee.
10 You would have an institutional advisory committee that
11 would make recommendations on this to the board of
12 directors. The board of directors would be represented
13 by -- there would be a group that would have votes, which
14 would be the large investment banks, the mid-sized ones,
15 the smaller ones. You would come up with a better-
16 informed answer. As time goes on, if you found that the
17 listing standards were too loose, you would tighten them
18 up. There would be a mechanism in place to make sure
19 that the hole was safeguarded. I think that is kind of
20 what got lost from the current for-profit stock exchange
21 model with 50 ATSEs and ECNs and stock exchanges all
22 competing for the same trade.

23 MR. GRAHAM: Greg?

24 MR. YADLEY: I would like to thank you both,
25 David and Vince. We have been reading with great

1 interest all of your articles. I think I have a clear
2 idea, David, about what you are talking about. A lot of
3 it seems to be modification of the applicability of
4 existing exchange-type standards, both from the SEC's
5 standpoint as market participants, how DTTC operates in
6 order to bring a market that better reflects the needs of
7 the issuer and the investors in these smaller companies.

8 I am less clear, Vince. I have read the ATS
9 rules, and I think I know what they are, but I don't
10 really know how they work in practice. So I am not sure
11 what is involved when we say we could start building from
12 that model.

13 Maybe, David, you are able to elaborate a
14 little bit, too, on this because just basic information.
15 There are, what, less than 200 ATSES? I think some have
16 multiple assets that they are qualified to deal in, but I
17 don't really understand the risk profile and how much
18 market making is involved in those or how much of it is
19 just a platform.

20 MR. SHILLMAN: Sure. Maybe I can give you some
21 general information on the ATS model. ATSES were
22 designed to be a lighter-touch regulatory regime for
23 businesses that effectively were performing the function
24 of an exchange, bringing together multiple buyers and
25 sellers.

1 Reg ATS, as Vince mentioned, requires
2 registration as a broker-dealer. That is a process that
3 takes, you know, six, six months or so. Plus, I think
4 what you were referring to is the business lines. Often
5 with the FINRA process, there will be a designation of,
6 you know, the type of business than the M&A will be
7 engaging in. If it wants to restrict it to a certain
8 business and then expand, it would have to come back and
9 get that modified.

10 With respect to the SEC process, there is a
11 notice filing with us that requires a description of the
12 ownership structure in the business. It is just not an
13 approval process. It is just a notice filing with the
14 Commission. Once that notice filing is made, then 30
15 days thereafter, business can commence.

16 So I want to be clear. There is nothing in Reg
17 ATS that restricts it to trading registered securities.
18 In fact, I think some of the shares post-Second Market
19 were registered as ATSES. So I think maybe some of the
20 issues around that that you were focused on were dealing
21 with who can trade and under what conditions, which
22 really may be more '33 Act issues.

23 There is nothing in Reg ATS itself that would
24 preclude unregistered securities from trading on an ATS
25 vehicle. There really is freedom for those who operate

1 the ATS to design them the way they want. So there is
2 nothing that would preclude an ATS or exchange from being
3 a nonprofit membership organization. There is nothing
4 that precludes in any particular business model. I think
5 some of the more intriguing regulatory issues around
6 small company stocks where there could be a regulatory
7 solution are around should regulatory steps be taken to
8 concentrate trading on certain venues. Right now, the
9 regulatory structure has been designed to encourage
10 competition. That was designed at a time when with
11 respect to the larger cap stocks, there was desire to
12 break up the monopolies of the New York Stock Exchange
13 and in AMEX.

14 So some of the issues that we have been
15 thinking about, you know, are the extent to which we have
16 the flexibility under the '34 Act to allow trading to be
17 concentrated on one or few exchanges so that incentives
18 can be created for liquidity providers.

19 Hopefully that gives you a sense of the
20 structure.

21 MR. YADLEY: No. That is exactly what I am
22 sort of getting at. It sounds like from what I know of
23 ATS, which is, admittedly, very little, there is a
24 structure in place. I think since the purpose of our
25 advisory committee is to provide comment to the SEC on

1 what we think the Commission and the staff can do, I am
2 wondering what specific kinds of things, Vince, we should
3 be thinking about that would allow this because I think,
4 you know, David has laid out a whole list of things that
5 from an exchange model, we need to think about and
6 evaluate which of them are necessary, which of them are
7 desirable, how they would fit together.

8 MR. MOLINARI: I appreciate the point, Greg. I
9 think when you look at it, it is the process of the ATS.
10 Certainly it is clear that you could transact
11 unregistered securities on the ATS.

12 I will tell you when we did our first ATS 3 and
13 a half years ago, it was a 14-month approval process for
14 a limited approval under 144(a) transactions. So if we
15 are talking about the ability to move to action and to
16 bring more participants to a marketplace using existing
17 regulatory structure, I think we have to create the
18 efficiency where that process is.

19 There was a time not too long ago, 18 years
20 ago, when there wasn't a timeframe for a broker-dealer
21 approval process to be done within. Right? So some of
22 those were taking 18 or 24 months. Then you have a six-
23 month process in order to get it done, either approve it
24 or not. So I think we need a similar mechanism in the
25 ATS process to say, "Here is the process. Here is the

1 window. Approve or disapprove the ATS within this
2 timeframe."

3 I think within that, there is a greater swath
4 of what you were approved for. So is there an approval
5 set that says, "Unregistered securities" as the approval
6 set that increases the amount of the stack that is
7 approved at one point in time?

8 I think when you then give that type of
9 guidance and the marketplace begins to realize that there
10 is a clear mechanism within our regulatory framework;
11 that is, broker-dealer; that is, FINRA SRO, which I think
12 helps perhaps give some of the states comfort, and then
13 you extend that using electronics, -- this is about using
14 the electronic connectivity and reaching out -- more
15 visibility, more participants, more eyeballs on the
16 product, some liquidity, greater liquidity, better price
17 discovery. So I think that becomes the process that we
18 can start today.

19 I think, again, going back, that is a bit of a
20 pilot program than we are looking at the venture
21 exchange. Do these grow up to become the venture
22 exchange when we know what the venture exchange is, the
23 rules of engagement? Do we learn things from this
24 expanded ATS process that makes the venture exchange
25 better when it comes to be?

1 I don't think they are certainly mutually
2 exclusive at all. I think they are hand in glove. Maybe
3 it is a bad analogy, but if we think back to
4 crowdfunding, 2011, I had a belief that said Title III
5 should be a broker-dealer activity pursuant to the
6 private placement designation of the broker-dealer.
7 Let's extend or fix that. I didn't necessarily think
8 that we needed a broker-dealer-like mechanism outside the
9 box.

10 So, having a little deja vu, saying, "Well,
11 let's utilize what we have today. Let's move to action.
12 Let's make people aware of it. Let's make market
13 participants know that it is there." That is well within
14 the SEC's purview to get that rolling, and I think that
15 begins the momentum to visit other things as we are going
16 along in conjunction with the venture exchanges.

17 Sorry. That is a long answer.

18 MR. YADLEY: No. Thank you.

19 MR. WEILD: This was a FINRA delay, though, 14
20 months. It was FINRA, right? It is not the SEC? Am I
21 right?

22 MR. MOLINARI: Absolutely, but it did take a
23 step back with the SEC to govern and say, "There is an
24 ombudsman." Okay. It is six months. Oh, the ATS
25 process?

1 MR. WEILD: Yes, yes.

2 MR. MOLINARI: Oh, yes. I think the SEC might
3 have a little bit of influence on

4 MR. WEILD: Yes, I think they do.

5 MR. MOLINARI: -- setting the stage for that.

6 MR. GRAHAM: Yes, John?

7 MR. BORER: I have two questions, one of which
8 is historical and maybe one of you would have the answer.

9 The other is to the point that was just made.

10 To the first one because it will be more
11 succinct, I recall four or five years back when the
12 NASDAQ had gotten approved and was going to be rolling
13 out a venture exchange, which they called -- I think it
14 was the BX Venture Exchange, which was

15 MR. WEILD: Yes.

16 MR. BORER: -- lower not for private securities
17 but for companies that did not qualify for listing on the
18 NASDAQ.

19 MR. WEILD: BX Venture.

20 MR. BORER: To my knowledge, I never recall
21 anything happening there, in spite of the fact of going
22 to several seminars put on by NASDAQ to explain to the
23 broker-dealer community what a great adventure was going
24 to be. Do either of you know what happened, if anything,
25 with respect to that initiative?

1 MR. WEILD: Well, I can tell you what I was
2 told by people at NASDAQ, which was that they had
3 acquired the Boston Stock Exchange. It was the old
4 Boston Stock Exchange SRO license. So they decided that
5 they were going to go into business and try and compete
6 against the over-the-counter market essentially and other
7 things. This is what I was told. So the SEC would have
8 to vouch for this one way or the other. They said that
9 they couldn't get an exemption from Reg NMS. So they
10 were concerned with the small volumes and everything that
11 it would be unprofitable. So it wasn't worth them
12 investing in. They were also limited in terms of who
13 they could list on the exchange. So they were only
14 allowed to list companies that didn't otherwise qualify
15 to list on NASDAQ. That is what I was told by NASDAQ.

16 MR. BORER: The second piece of my question
17 goes to the conversation which just took place, which is
18 the difference in mandate between the SEC and the various
19 things that they have to do and FINRA. Being in a
20 broker-dealer, I am subject to FINRA oversight. It does
21 not seem in my experience that FINRA is expansive in its
22 desire to promote greater levels of flexibility;
23 activity; and capital, ability to raise capital, under
24 the way that they currently look at things.

25 I think it was just mentioned with respect to

1 ATS. At the SEC, it is a filing; whereas, at FINRA, it
2 is somewhere between one and two years, as I understand
3 it. Do either of you want to comment on that? Is that
4 one of the issues with respect to expanding the ability
5 and giving small firms perhaps, maybe not just the big
6 ones, the incentive to try to venture into this pool?

7 MR. MOLINARI: I think we are limiting the
8 conversation to the ATS. Two years would be a big of a
9 stretch but certainly 12 months either side of that would
10 not be unusual at this point.

11 Our experience with FINRA through the
12 rulemaking process since the JOBS Act has been very
13 encouraging. So I just think this is something that
14 actually helped FINRA in the process because, no
15 question, we have to deal with the issue. Everybody
16 recognizes it. Whether it is FINRA, SEC, or the states,
17 we have a tremendous pent-up demand of private
18 securities, unregistered securities that have been put
19 into the system that have no ability for a structured
20 regulatory framework for liquidity. That speaks to
21 everyone's concerns for investor protection, and it
22 speaks to everybody's concerns of feeding the system new
23 capital to continue the cycle.

24 I don't see that as a real friction point with
25 FINRA. I think we might need a little encouragement, but

1 I don't think it is a huge barrier to get around or get
2 through, rather.

3 MR. WEILD: Without naming names, there are
4 people that served on the Commission at the time of
5 Arthur Levitt who have shared with me that one of the
6 interests in driving competition in markets was this
7 basic thought process. I don't think this was made
8 public. By depriving salesmen of the ability to earn a
9 living selling securities, you could essentially end
10 sales practice abuses. I have had subsequent
11 conversations where we have talked about putting some
12 incentive back into it. Some of the same people, say,
13 you know, are concerned about that.

14 So there is no question that when you have an
15 incentive to sell, there will be sales practice abuses.
16 So the enforcement side needs to, you know, be pretty
17 vigilant. You get on a slippery slope in businesses
18 when, all of a sudden, you decide that brokers shouldn't
19 market stocks, when real estate brokers shouldn't market
20 houses, when software salesmen shouldn't sell, when car
21 salesmen shouldn't sell. I think that there is, at least
22 with some individuals historically, some of that
23 philosophy that may have helped drive us to where we are
24 currently.

25 MR. GALLAGHER: Can I mention something about

1 this? Sorry. Just to John's question, which I think
2 David answered well on the NASDAQ BX venture, I think
3 when we talk about the venture exchange idea now, it is
4 more like, to use movie analogies, "Field of Dreams,"
5 right? You build it, and hopefully they come. NASDAQ
6 built it, something, before we did, right? They
7 essentially front-ran the regulatory structure.

8 To David's point, these things that we talk
9 about, non-UTP, non-NMS, I know you talk about order-
10 handling rules and all sorts of other things. They are
11 in place, right? They are the existing potential burdens
12 that we need to analyze that I think the BX Venture
13 failure in some regard, the fact that it is not up and
14 running and vibrant, proves out the theory that we need
15 to remove these impediments. We need to build the field
16 before they come. The private market is not in a
17 position, unfortunately, as they are in so many other
18 ways, to take us doing nothing as a key to create their
19 own solution. We have got them boxed in pretty well
20 here.

21 David, one last point. I think on AMEX --
22 maybe Dave Shillman is a better one on this -- if I
23 remember correctly, I think a significant chunk of their
24 failure had to do with the fact that they were not blue
25 sky-exempt.

1 MR. WEILD: Yes, but you know NASDAQ wasn't
2 blue sky-exempt either for a long time, right?

3 MR. GALLAGHER: Well, when you are running two
4 tiers, though, right, I think NASDAQ was a true
5 alternative, but when you have the AMEX million

6 MR. WEILD: Yes.

7 MR. GALLAGHER: -- and then the AMEX venture
8 tier, you do get into an interesting situation.

9 MR. WEILD: We will get into a long discussion.
10 One of the things that happened with the AMEX because it
11 got squeezed, it was a greater incentive to list things
12 on NASDAQ for the small companies. So the street did.
13 They pushed in that direction. The New York Stock
14 Exchange, being the big board, attracted everything.
15 AMEX was getting squeezed in the middle.

16 Also, you know, if you look at what people did
17 with the specialist model, specialist model worked much
18 better on the New York in terms of quality of markets
19 because they were subsidizing small cap liquidity with
20 big cap excess profits. It was understood through the
21 allocation system that that was in the interest of -- I
22 saw with Dick Grasso having these conversations and
23 Richard Bernard, who was the general counsel. If you
24 look at the AMEX, they didn't have a supply of big cap
25 stocks. So they didn't have the subsidies. So the only

1 way that the specialists could make the money was by
2 getting in front of the stocks. So, as a consequence,
3 really, instead of improving the quality of markets for
4 micro cap stocks, they actually got a reputation for
5 picking people's pockets.

6 MR. GRAHAM: Charles?

7 MR. BALTIC: Thank you, David and Vincent, for
8 the presentations.

9 I want to direct this question in the first
10 instance to you, David, about the significant decline in
11 the number of companies going public structurally over
12 decades now. It is very telling. The idea of a venture
13 exchange or venture exchanges is intuitively very
14 appealing to create a specialized market geared for small
15 cap companies and getting them into the public markets.

16 I wanted to go back to something that you said
17 when you addressed ETFs and index funds because, really,
18 some of the newest developments in the market are the
19 amount of money going from active management to passive
20 management. These vehicles are essentially information-
21 agnostic. It seems like one of the main premises of the
22 success of a venture exchange would be getting
23 information to the market, particularly for smaller
24 companies that are not well-understood or well-followed
25 and where there is the opportunity to create real value.

1 So I think one of your slides said no to ETFs,
2 but in practice, it would be very hard to walk back from
3 where we are in the investment world today. What
4 specifically could a venture exchange do to address that
5 fundamental change in the market and so much money going
6 towards passive investment, effectively commoditization
7 of investment decisions?

8 MR. WEILD: Well, I mean, I think that a simple
9 thing that they could start doing is mandating that all
10 exchange-traded funds and index funds have to put
11 standing orders out there on transactions because
12 otherwise you are just depriving the whole market of a
13 supply of capital that goes into the company's treasury
14 that actually helps to create jobs. I mean, it is back
15 to my point of if 100 percent of all trading was ETF, 100
16 percent of all ownership was ETF, and index fund-related
17 there would be nobody left to put money to buy new issue
18 equities, you know.

19 I do think you can mandate that there isn't
20 going to be any of that activity permissible in a venture
21 exchange and if not because -- I believe academics talk
22 about two types of information. I don't want to get in
23 trouble with Commissioner Piwowar, who has his Ph.D., but
24 here we go. I am going to do it anyway. Information
25 mining strategies and information

1 MR. PIWOWAR: There will be a pop quiz when you
2 are done.

3 MR. WEILD: Okay. Here we go. Information-
4 mining strategies and information additive strategies.
5 Computer-based systems, which are much less costly to
6 implement, are all the information-mining strategies,
7 which is what you are seeing, you know, grow, grow, grow.
8 That includes ETFs and index funds, then the information
9 additive strategies, which I would argue are the things
10 that fundamental sell-side research analysts are doing,
11 fundamental buy-side analysts, the people business, which
12 is going to be innately more costly to effect.

13 So stocks that really require information
14 additive strategies or the invisible, more
15 technologically complicated smaller capitalization
16 stocks. As you squeeze that out of the market, then
17 almost by definition, you are going to end up with
18 pricing anomalies. It is going to start to undermine
19 efficient allocation of capital if it hasn't already.

20 So while it is very easy to get up on your
21 soapbox or vanguard and preach the benefits of index
22 investing and the lack of value of active managed
23 portfolios, the problem with it is that if you take it to
24 its logical extreme, you ultimately have massive
25 disconnects in the way that stocks trade. They don't

1 trade efficiently any longer.

2 MR. MOLINARI: Charles, may I just add to that
3 slightly? I think it is a fundamental reeducation of our
4 American investor. I think going back, we have lost all
5 connectivity of what it means to be an investor. We have
6 forgotten the process that capital going to small and
7 emerging companies creates jobs. That gives them the
8 fuel to grow. I think we have been very focused on the
9 aspect of the stock price du jour, the tick. As we have
10 had more and more electronics over time, chasing
11 inefficiencies of markets, they become more efficient.
12 Margins compress and closer and closer. So I think we
13 have eroded ourselves. I don't want to use your analogy
14 again of the flesh-eating amoeba, bacteria, but,
15 effectively, that is what it is.

16 I think it is part of reeducating America that
17 capital put to work is investing in companies. It is not
18 just about the transaction. I think that is part of what
19 we look at. We call it actionable knowledge at Gate
20 Global Impact. The more information and knowledge that
21 we could put into the marketplace, the better protected
22 that investor is going to be because they understand what
23 they are buying, but they understand the process of what
24 it means to be an investor.

25 MR. GRAHAM: Commissioner Piwowar?

1 MR. PIWOWAR: Yes. Great. Thank you both for
2 being here, both Vince and David. David, I think it has
3 been three, four years since I saw you on the Hill. You
4 had this crazy idea that we should consider widening the
5 tick size for small cap companies. Just due to dogged
6 determination, he walked around with his report and his
7 charts and everything. We are actually on the cusp of
8 actually doing that. So great to see you again.

9 MR. WEILD: Thank you.

10 MR. PIWOWAR: It looks like you are applying
11 the same sort of determination for venture exchanges.
12 You have obviously thought a lot about these.

13 One of the things that is not on here -- and
14 sort of I was looking through your slides; I apologize
15 for not being here for your presentation -- that has been
16 talked a lot about in the market micro structure
17 community and with the academics is perhaps allowing
18 issuers -- you talked a little bit about this with
19 Commissioner Gallagher about, you know, in the old days,
20 you know, the specialists, there would be cross-
21 subsidization from the large stocks to the small stocks
22 and how do we incentivize market makers to make a market
23 in this stock. One of the things that the academics said
24 is, "Well, why don't we allow issuers to hire their own
25 market makers and pay them directly?" Is that something

1 that is on your radar screen? Is that something that you
2 are thinking about would be potentially something for us
3 to think about in the context of venture exchanges?

4 MR. WEILD: Well, there is some evidence from
5 the U.K. market, where they pay our market makers, that
6 it actually improves liquidity. I think that my sort of
7 strong preference is that I would rather see market
8 makers have some affirmative responsibilities. I would
9 rather see the incentives out on the street because I
10 think that a lot of these small cap companies need to be
11 writing checks like they need a hole in the head. I
12 would rather see, if you will, the support come from the
13 market itself.

14 That said, when you look at the data, it is
15 very clear in that U.K. model that it actually did
16 support liquidity. So I am a pragmatist. At the end of
17 the day, I want to do everything that I think is going to
18 help, you know, raise capital and get America back into
19 business. If that is part of the arsenal, then so be it.

20 MR. GRAHAM: Okay. Shannon?

21 MS. GREENE: Real quick. So my whole point of
22 being on this committee is because I come from a very
23 small public company, \$90 million market cap. So I guess
24 it would be maybe a good place to state the point that
25 for all of the world on how to get more IPOs and get more

1 companies to go public, small companies, you know, I
2 guess I would like to remind the committee that for every
3 IPO we get done because of the JOBS Act or because of
4 whatever else we can do to make that process easier,
5 there are existing companies that are living in the
6 public market that are looking for ways to get out of it
7 simply because there is no purpose.

8 We are one of those. I mean, I will be honest.

9 I get a call every month when I talk to investors, "Why
10 are you even public?" So we can increase the IPO market,
11 but at the end of the day, we may not increase the total
12 number of public companies because the guys like us are
13 going to fall out. For every one you add, we are going
14 to look at a way to get out of it just because of, you
15 know, the world as it is now.

16 So I just interject. I am all for IPOs. I am
17 all for growing companies. I am all for more jobs, et
18 cetera, et cetera, but this is kind of refreshing, David,
19 to hear. You know, I am sitting here thinking that this
20 might be something that would actually benefit us, a
21 venture exchange of some sort, not the redheaded
22 stepchild, which AMEX kind of became. I mean, that is
23 the way we went public, but when you told people you were
24 on the AMEX, they kind of looked at you with this kind
25 of, you know, "Sorry you couldn't qualify to be on a real

1 exchange. So you are on the." You know, so we live in
2 that world all the time we are on NASDAQ now.

3 NASDAQ, as you know, is going to an all-
4 inclusive listing fee arrangement. So you pay one fee to
5 do whatever you want, your annual fee, plus additional
6 shares or whatever. Well, our fees are going up 38
7 percent for nothing because we don't list additional
8 shares. We don't change corporate names. We don't do
9 all of those kinds of things. So small public companies
10 are really getting squeezed, and writing additional
11 checks for whatever is a painful process.

12 So I just raise the point that for every IPO we
13 enable for small companies to get there, you are going to
14 see them fall. I think we are going to continue to see
15 them fall off on the back end because it is not worth
16 what we are dealing with these days. So I just have to
17 interject.

18 MR. WEILD: I would love to see the
19 improvements for the venture exchange model up to \$2
20 billion apply to already public companies. To your
21 point, this is the problem with the for-profit exchange
22 model I ran with listings business global. Where they
23 are increasing, you are increasing those shareholder
24 fees, believe me, somebody has got their slide rule out.
25 They have figured out what they can do to their earnings

1 per share. That is exactly why that is happening. You
2 are a slave to your shareholders, instead of being a
3 slaved to your listed companies, your institutional
4 investors, and your member firms.

5 So the public policy, you know, sort of balance
6 the utility aspect of the markets was taken out when we
7 converted to a for-profit exchange model in the interest
8 of driving competition. So we just have to get the
9 balance back in. I think if we do, again, we will be
10 back in business.

11 I think it is horrible for this country when a
12 \$90 million market value company sits there and says, "I
13 want out of the market." You know, this is what we are
14 hearing. This is not unique to you. It is sort of like
15 you get in there, you do your best, you work your tail
16 off, the costs are too high, you are throwing in the
17 towel. You know, that is not how we are going to be
18 successful as a nation if that experience is as
19 widespread as we think it is.

20 MR. GRAHAM: Okay. Thank you, David.

21 We are fast running out of time. I know that
22 people have planes, et cetera, to catch. So I want to
23 thank David and Vince. It was very helpful. Good to see
24 you both, and I suspect we will see you again before too
25 long.

1 MR. MOLINARI: Thank you. Thank you for having
2 us.

3 MR. WEILD: Thank you, everyone.

4 MR. GRAHAM: Okay. Our last few minutes.
5 First, we want to go back to the latter half of this
6 morning, when we talked about 4(1-1/2) and some of the
7 other issues that Annemarie addressed. Just quickly, I
8 think that the whole notion of codifying the so-called
9 rule 4(a)(1-1/2) is a good idea. I think it is a small
10 but important step, improving liquidity for small cap
11 companies for all of the reasons that we looked at this
12 morning. So the first thing I want to do is suggest that
13 we make that recommendation.

14 Any comment on that? Yes, DJ?

15 MR. PAUL: The only comment I would make is
16 that as we frame it and this is probably the only thing
17 I possibly disagree with Annemarie about, her
18 presentation this morning, is that I don't believe that
19 this needs to be done at the legislative level. I
20 believe the SEC does have the authority to do this. So
21 it is appropriate for us to recommend it and for the SEC
22 to act on it. So I would simply ask that when we come up
23 with worrying that we state that.

24 MR. GRAHAM: Yes.

25 MR. PAUL: That is all.

1 MR. GRAHAM: I would agree with that. So we
2 will come up with wording, but can I have a motion?

3 A PARTICIPANT: So moved.

4 MR. GRAHAM: Second?

5 A PARTICIPANT: Second.

6 MR. GRAHAM: Any more discussion?

7 (No response.)

8 MR. GRAHAM: All those in favor.

9 (Chorus of ayes.)

10 MR. GRAHAM: Opposed?

11 (No audible response.)

12 MR. GRAHAM: Okay. Done. This afternoon's
13 topic, you know, obviously was very broad. There are a
14 lot of subissues associated with it. I think that the
15 notion of a venture exchange is, you know, again, as I
16 said earlier, something that I think is a good idea and
17 something that the committee as formerly constituted
18 thought was a good idea. So we have already gone on
19 record once in so many words.

20 I think it is important for us as a committee
21 to think about specifics, as more than one of you
22 mentioned, and what kind of recommendations might we be
23 in a position to give that might really be useful in
24 terms of guidance, then kind of understanding the way
25 this hits our various constituents.

1 So I think that is something that we are all
2 going to have to keep thinking about. We are not going
3 to resolve it in the next three minutes. We will put it
4 on the table, and we will pick it up at our next meeting,
5 which I don't think we have scheduled yet. Have we? I
6 am sorry. June 3rd?

7 A PARTICIPANT: Yes.

8 MR. GRAHAM: Okay. It must be on my calendar
9 somewhere. Good. So that is our next meeting. So what
10 we will do is put together the accredited investor
11 recommendations, the final version, that we talked about
12 this morning that we actually passed. We will get a
13 draft of the Reg A+ recommendation out to people to take
14 a look at, then a draft of the 4(a)(1-1/2). And we are
15 putting venture exchanges on the table but not really
16 table. We are still thinking about it. We are going to
17 keep up the dialogue.

18 Catherine?

19 MS. MOTT: Stephen, to help me understand the
20 venture exchanges, I would really like to hear from the
21 SEC what it means because I read the recommendations
22 David put here that it would require maybe a separate I
23 guess division within your organization. What was it?
24 Should be chartered separately by the SEC in order to
25 sustain a small cap, you know. So I would just like to

1 hear what it means to you as an organization to implement
2 this. I would just be curious to understand it, what it
3 means.

4 MR. HIGGINS: I am not exactly what it

5 MS. MOTT: He said yes, a separate venture
6 exchange division at the SEC listing rules disclosure.

7 MR. HIGGINS: You are looking at the article
8 that was distributed just a couple of days ago?

9 MS. MOTT: Yes.

10 MR. HIGGINS: Yes. I thought that was a great
11 article. I thought that, at least as far as his ideas
12 were concerned, he did a good job of laying it out.

13 One of the questions I have, too, is, really,
14 what does that mean as a practical matter?

15 MS. MOTT: Right.

16 MR. HIGGINS: I think that is what we have to
17 kind of get behind before we can kind of think about what
18 in the way of specifics we might even think about we want
19 to recommend.

20 MR. GRAHAM: Unless Keith has like a two-minute
21 answer or something, I think that is probably something
22 that we can

23 MR. GOMEZ: Stephen?

24 MR. GRAHAM: -- we should look at in detail the
25 next time around, but if you have something to say right

1 now?

2 MR. GOMEZ: One thing to throw out that might
3 be helpful to the committee is I know there is a lot of
4 three-syllable, three-letter acronyms and things like
5 that. It might be helpful maybe at the next meeting to
6 have a more fulsome presentation maybe by SEC staff, if
7 possible, kind of explain some of these concepts. I know
8 there were a lot of recommendations as to amend this
9 regulation or that regulation. It might be helpful for
10 the committee to maybe get a better understanding of what
11 those regulations are and which ones. That way you can
12 make a more informed decision.

13 MR. GRAHAM: Yes.

14 MR. GOMEZ: So that will be helpful. Then we
15 could work on that.

16 MR. GRAHAM: You know, having that context
17 would be great. And we could have a test after lunch.

18 (Laughter.)

19 MR. GRAHAM: Thank you all for coming. I think
20 you are a great committee. I think it was a good day,
21 and I appreciate your input. So, with that, I think we
22 are adjourned.

23 (Whereupon, at 3:29 p.m., the meeting was
24 concluded.)

25 * * * * *