U.S. SECURITIES AND EXCHANGE COMMISSION

SMALL BUSINESS CAPITAL FORMATION
ADVISORY COMMITTEE

Tuesday, September 19, 2023

10:00 a.m.

U.S. Securities and Exchange Commission

100 F Street, N.E., Washington, D.C.

Station Place 1 Multipurpose Room

PARTICIPANTS:
Erica Duignan, Chairman

Wemimo Abbey
Donnell Baird
William M. Beatty
Stacey Bowers
George Cook
Vincent Cordero
Marcia Dawood
Greg Dean
Bailey Devries
Bart Dillashaw
Herbert Drayton, III
Diego Mariscal
Laura Niklason
Davyeon Ross
Jasmin Sethi
Aren Sharifi
Marc Oorloff Sharma
Dennis Sugino
Sue Washer

C O N T E N T S

P R O C E E D I N G S

Opening Remarks

MS. DUIGNAN: Call to order. I want to extend a warm welcome to everyone, including those members that are joining us remotely. It's great to see everybody here and by WebEx.

We also appreciate all the members of the public who have tuned in to watch the meeting via the webcast on SEC.gov.

Courtney, do we have a quorum for this meeting?

MS. HASELEY: We do. And if I may at this time, I'll just start by giving the standard SEC disclaimer that all of the members of the Office of the Advocate of Personal Business Capital Format and other SEC staff are very happy to be here today.

But on behalf of myself and the SEC staff, I want to state that any views that the SEC staff expressed today made in each staff's members official capacity and do not necessarily reflect the views of the Commission, any of the Commissioners, or any of our other colleagues on staff.

MS. DUIGNAN: I apologize. I've no idea. I've never seen that happen. It must be a Microsoft Word thing. I don't know. Great, Courtney. Okay, wonderful. So, apologies for that.

So, my name is Erica Duignan, Committee Chair, and for many of us, including me, this is just our second committee meeting, so please excuse any technical snafus, but I was greatly impressed by the thoughtful discussions that we had at our last committee meeting in June, and we're all really looking forward to diving deeper into them today.

So, in developing today's agenda, the officers and I took input from that June meeting and decided to focus on two main areas that seem to garner a lot of interest.

So, the first part of the morning's agenda focuses on the role that smaller venture capital funds and investment firms play in supporting small and growing early stage companies, particularly those with underrepresented founders.

Yet the capital that LPs are investing in smaller funds and emerging managers is continuing to be a declining sliver of the overall pie. So, we'd like to dig into some of the reasons for this and possible solutions as to how we can possibly correct it.

So, we have two speakers this morning who will speak to decision making, the process, and challenges at the asset allocator level, and we hope that their perspectives will spur discussion by the committee on whether there are ways to bring more minority founders into our capital ecosystem.

Encouraging investments in smaller funds and more diverse funds with emerging fund managers bringing new perspectives and diverse GPs to the check-writing community and they are often more well suited to driving capital to those early-stage companies.

And in the afternoon, we're going to talk about alternative models for companies that are seeking more long-term growth capital.

We'll start by hearing from the team at the Department of Treasury, who has been rolling out the $10 billion public/private/state business credit initiative. It will be really interesting to hear what approaches various states are taking there.

Also this morning, committee member Bailey DeVries will talk about the Small Business Administration's recently adopted role reforms aimed at increasing access to private equity and debt capital for underserved small businesses and startups and diverse and emerging fund managers.

We're going to leave it to Bailey to explain the nuances but effectively the SBA has expanded the Small Business Investment Company program known as SBIC to introduce two new SBIC licenses to strengthen, diversify, and expand the program's network of private market financing partners as part of a broader effort to help fill funding gaps and unlock potential in underserved small businesses.

It's a truly exciting and meaningful change for both investors and the underrepresented founders that we are excited to get more capital to, and we're all looking forward to learning more about the program.

But before all of that, we are so pleased to have Chair Gensler, the commissioners and Erik Gerding, director of the SEC's Division of Corporate Finance join us. We really appreciate you being with us this morning. Chair Gensler, would you like to start with your remarks?

MR. GENSLER: Thank you so much. I'm pleased to speak with the Small Business Capital Formation Advisory Committee. As is customer, what's noted by one of my colleagues, my views are my own as chair and I'm not speaking on behalf of my fellow commissioners or staff.

I really -- so pleased to welcome and thank the committee's newly selected leadership team for taking on -- so you cannot hear me? I'm guessing there's a technical malfunction.

MR. ROSS: Yeah, we can hear you. This is Davyeon.

MR.GENSLER: You can hear me?

MR. ROSS: Yes, I can hear you.

MR.GENSLER: Terrific, terrific. And I'm back from the Matrix or I am back in the Matrix. All right. Terrific. I'm pleased to speak with you all today, and as was said by my colleagues, my views are my own as chair, and I'm not speaking on behalf of my fellow commissioners.

I'm just so pleased to welcome and thank the committee's newly selected leadership team. You've got a lot of things going on in your lives outside of this committee.

You signed up to help advise and be part of the committee, but now you've taken on yet another role as chair, as vicechair, as secretary, as assistant secretary, but Erica, Sue, Jasmine, Davyeon, I can't thank you enough for taking on these roles of leadership and helping out the committee, helping the committee advise us, the commission.

I'm pleased that we'll hear from you today, but first, you're also going to hear from Erik Gerding, as you said, the director of the Division of Corporate Finance, and I know Erik will share with you some of the wide-ranging work our agency does on behalf of small businesses.

And small businesses, as we all know, make up such an important part of our economy. It's often through these small businesses that those who have a dream or want to take a risk can make a go for it.

And that's why it's critical that the capital markets help facilitate capital formation for businesses, small and large, and that our agency helps small businesses navigate the capital-raising process.

And sometimes, those pathways that they're using directly are in the capital markets or in the public capital markets, but often, it's really accessing capital that's not in the public markets but may well be in what's called the private markets or even in the bank credit markets and the like.

And we help -- we help at our agency pathways for small businesses to help navigate this process such as through our various exemptions in our registration process, Regulation D, that many of you know, Regulation A, Regulation Crowdfunding.

We also offer resources to small businesses such as through the dedicated staff with the Division of Office of Small Business Policy, as well as our Office of Advocate for Small Business Capital Formation. I'm sure you know these teams, and you'll get to know them better over time as committee members.

We benefit, though, from your insights from the frontlines what more we can do from resources or rulemaking to beyond.

Again, this sometimes relates directly to something we're doing around the capital markets, or sometimes it's indirect, even if the fundraising that small businesses are doing is from banks or credit funds or private funds in the capital markets.

We also benefit from discussions like they're going to have today. I understand your morning sessions taking up the important topic with regard to limited partners who invest in smaller venture funds, and we look forward to hearing your thoughts from that and that your afternoon discussion is going to be about alternative funding options for small businesses. And given how important nonequity funding can be for small all businesses, particularly early on.

I look forward to your perspective on these topics. I also want to thank today's guest speakers from both -- I understand you have some speakers from the venture capital field and from colleagues across the government in the U.S. Department of Treasury for joining us.

And so, back to you, Erica, and I'm sure some -- I see some of my fellow commissioners here.

MS. DUIGNAN: Thank you so much for your remarks, Chair Gensler. We really appreciate it.

I'm now honored to invite Commissioner Pierce for remarks.

MS. PEIRCE: Thank you, Erica, and I echo Chair Gensler's, thanks to those of you who have taken on leadership positions.

This is actually a lot of work, but it's important work, so grateful that you are willing to take the time and grateful to all of you on the committee who have been devoting your time to this committee. It's really, again, very valuable for us.

You will typically not see me sitting through the whole sessions here but I do watch them after the fact, so do know that what you're talking about and the recommendations you make are important to all of us on the commission.

You have a full agenda today. I'd like to focus specifically on this first discussion around limited partners investing in smaller venture capital funds. And one thing that prevents that from happening potentially is if there are no small venture capital funds because the regulatory barriers to entry are high, and that's something that I've been thinking a lot about recently. And most specifically because last month, we finalized a rule for private fund advisors.

It's a pretty sweeping rule and imposes many new obligations. And there are many aspects of it that prevented me from supporting it, but one primary objection that I had was that this rule, I think, will have deleterious effects on the ability of small fund advisors to even get their businesses up and running. And there may be insurmountable barriers to entry because of the regulatory -- the new regulatory overlay.

The commission's economic analysis did acknowledge that the rules compliance cost could result in smaller advisors leaving the market, but argued that smaller advisors could sidestep the rules cost by reducing their assets under management below the required SEC registration threshold.

In my view, urging smaller advisors worried about regulatory burden to shrink undermines rather than fosters the kind of competition we're looking for here.

The commission certainly doesn't intend to formulate rules that disadvantage smaller advisors but we can be insensitive to how individual rules harm advisors and certainly the whole collection of rules together, the aggregated, regulatory burden, how that affects smaller advisors.

Occasionally, we'll stagger a compliance date, but we have tended to refuse to accommodate unique challenges faced by smaller advisors.

Last week, the Investment Advisor Association petitioned the commission to amend the rule that calls on the commission to revisit the definition of smaller advisor that it uses when considering how a proposed rule will affect small advisors.

The commission currently treats small investment advisors, those that have less than $25 million in assets under management, which is lower than the threshold to register with the commission.

So, typically when the commission is considering how its rules will affect small advisors, it concludes that there won't be much affect because there are so few advisors that fit within that category.

The IIA's rulemaking petition calls for a new definition of small advisor based on the number of employees. Smaller asset managers I think might be more willing to work with smaller startups which I think will be part of your discussion today.

The goal, as Erik has said, is to open the capital markets to bring more people into those capital markets to -- both as investors but also as founders who don't recognize maybe the potential benefits that they can draw from being part of the capital markets.

And so, I think having smaller advisors who are willing to make smaller investments can really be transformational for founders and also for the LPs who get to be -- participate in those smaller startups.

I do think that regulation is one of the barriers to entry. As Sue was mentioning to me before, that's their other barriers to entry, it's hard for investment advisors to invest small amounts in small companies.

But I do think the regulatory barriers are there, and I would love to hear your thoughts on that. What the commission can do to foster opportunities for smaller venture capitalists and of equal importance, what the commission should undo.

So, thank you for all your time and energy that you're committing today and to the broader project of being on this committee, and thank you to all the panelists as well.

MS. DUIGNAN: Thank you, Commissioner Pierce for those very insightful remarks. We're all excited to learn a lot more about the new private fund rules as well. And with that, I am pleased to invite Commissioner Crenshaw for remarks.

MS. CRENSHAW: Good morning, Erica. Thank you for that. It's a pleasure to be here. And as my fellow commissioners have mentioned, always benefit from the lively discussions and presentations put on by the committee and its speakers, and today should be no exception.

And the first discussion, as you've heard already, will focus on investors and smaller venture capital and emerging fund managers, those managers more likely to support smaller early stage businesses, including diverse small businesses.

While the capital raised by large sponsors and private funds continues to grow overall, the market share going to smaller and emerging funds appears to be shrinking. This is an area of concern for me and one that I've spoken about in the past.

It appears to me that some of the policy determinations made by this agency, among others, have promoted a landscape that allows large, private issuers and their fund investors to grow exponentially, potentially at the expense of smaller, emerging and potentially more diverse businesses.

Today's discussion will also turn to the lack of diversity at the checkwriter stage, an area that we have received counsel on in the past and one where I think there's a good deal more that can be done. I look forward to your thoughts and considerations on those subjects.

And the afternoon's discussion will focus on alternative funding options for small businesses, a conversation that I hope will be informative to members of our entrepreneur community.

Finally, I want to mention I was not able to join the committee's last meeting, so I do want to take the opportunity to welcome the new committee members and to thank you in advance for your critical service for the varied experiences you bring to our conversations and for your considerations and ideas.

I want you to know that the recommendations that you present to us and the discussions in which you engage are a deeply important part of our decision-making process.

And as you've heard from my fellow commissioners, and I suspect we'd all agree that the success of the small U.S. businesses is inextricably tied to the overall success of our country and economy.

So, the challenge for this committee is a great one. How can we increase access to capital for our nation's small businesses while ensuring that we maintain robust protections for those investors that make those small businesses possible.

I encourage you to come up with new ideas, present new voices and new perspectives. Tell us something we haven't heard before. Help us bridge gaps where they may exist and build common ground for new and better regulations.

You're going to have to confront difficult problems like the ones that are being discussed today, as well as many others that you will discuss in the future.

I encourage you to approach those problems with the innovation and creativity of the small business community that you represent and serve. Your order is tall, but I know that you are all up for it.

So, I'm looking forward not just to today's conversation, but to the work that we will see from this committee moving forward. Thank you.

MS. DUIGNAN: Thank you, Commissioner Crenshaw for some very thought provoking and valuable ideas. We're excited to be inspired by your statements. And with that, I'd like to invite Commissioner Lizarraga for remarks.

MR. LIZARRAGA: Good morning, and thank you, Erica as well as the other members of the committee for your time and input today. On your agenda today are panels of a particular interest to me.

The first panel delves into who is investing in the funds that support early stage companies and ways to encourage more investments in those companies.

And the second panel addresses alternative funding options for small businesses that don't have the high growth model that VC funds generally seek and that need different avenues for raising capital outside of traditional equity investments and bank financing.

As the committee members know so well, support for small businesses is critical given their essential contribution to the creation of new jobs in our country.

The last 25 years, small businesses have accounted for over 60 percent of new jobs created. Small businesses generally have minimal collateral and may lack sufficient earning history, tax returns, or performance track records for traditional bank underwriting.

Better capitalized emerging fund managers that support early stage companies can be one solution. But in recent years, less funding has flowed to these vehicles, as LPs opt to write larger checks to favor more established, less diverse companies.

Incentivizing these investors to take a look at emerging fund managers and smaller VC funds will be crucial to expanding capital to underrepresented of the entrepreneurial ecosystem.

I look forward to hearing your ideas about potential pathways forward. Over the past several years, global investor demand for sustainable investing has translated into trillions of dollars flowing into sustainable or ESG focused funds. These are not altruistic donations. They're a product of investor-driven interest.

In the same vein, there is untapped demand for investments in smaller businesses that can diversify investors' portfolios, offer exposure to the wider variety of business types in geographic regions, and offer competitive returns while also providing greater opportunities for diverse entrepreneurs.

All of this boils down to finding the best ways of tapping into that demand. It's my hope that today's conversation will yield innovative solutions and forward-thinking ideas that inform efforts to move us closer to that goal.

Thank you again for your service and for your contributions to today's discussion.

MS. DUIGNAN: Thank you so much, Commissioner, we really appreciate the insight.

I want to let everyone know that Commissioner

Uyeda has a conflict this morning, but he will join us for remarks this afternoon, which we're looking forward to.

So, thank you so much, Commissioners. We really appreciate your time.

Next, we are pleased to hear from Erik Gerding, director of the SEC's Division of Corporate Finance.

MR. GERDING: Thank you all for having me. Thank you, Erica. I'll give the disclaimer again because I don't want to forget.

The views I express today are given in my official capacity as director of the Division of Corporation Finance and do not necessarily reflect the views of the commission, any commissioners, or members of the staff.

What you're all talking about today is very personal to me. I am the black sheep of my family. I am surrounded when I go home by entrepreneurs.

So, I have a front row seat to looking at how entrepreneurs and small business owners deal with risk and deal with the everyday struggles including raising capital and it is very, very eye-opening to watch the struggle.

So, I'm also the only non-native Spanish speaker in my household, so the intersection of diversity and capital formation is very, very close to me personally.

Before I became division director, I served as deputy division director and before that, I was at the University of Colorado as a law professor. I do not know Coach Prime. I've never met him, so don't ask me. But once I left, I had to bring somebody with, you know, a healthy sense of self-confidence to replace the vacuum.

I also was a law professor at the University of New Mexico and before that, I practiced in New York and Washington, D.C. with a large law firm, including exempt transactions.

So, I've seen a lot of the work that you all do, a lot of the questions that you all are confronting up front and personal from a number of different angles.

Let me give you a little bit of background on what Corp Fin, the Division of Corporation Finance does. We are the crown jewel of the SEC. Why can I see that? Because none of the other division directors are here, so I can get away with it.

If you had to have a tagline, we are the disclosure division. What we do is we work to provide investors with the critical material information they need to make informed investment and voting decisions and to facilitate capital formation. Corp Fin has two main functions.

First, we review and comment on filings by public companies, that public company -- we also provide policy interpretations and guidance to the public and to the commission.

Let's talk about that first function that we have. We review on public company filings. This is the job of our large disclosure review program, or the DRP. The DRP oversees corporate disclosure of material information to the investing public.

We have nine industry offices. I have to write them down because I don't want to forget any of my offices or I'll hear about it later in the day.

Number one, real estate and construction two, life sciences, manufacturing, trade and services, technology, energy and transportation, finance, crypto assets, which is a new office, as well as a new office of industrial application and services.

By breaking our disclosure review program and our work on public companies down, we really develop the expertise to deal with disclosure issues that may be unique to particular industries.

The disclosure review program selectively reviews filings made under the Securities Act of 1933 and the Securities Exchange Act of 1934 to monitor and enhance compliance with applicable disclosure and accounting requirements.

As required by the Sarbanes-Oxley Act of 2002, I remember when that was passed, and now I feel old, the division undertakes some level of review of each reporting company at least once every three years and reviews a number of companies more frequently.

In addition, the division selectively reviews transactional filings including the documents that companies file when they engage in public offerings, business combination transactions, and proxy solicitations. During the course of any particular review, the staff may provide a company with comments on that particular filing.

We also have that second function that we do, which is to provide policy interpretations to the public and the commission. And this is in another part of the division, the legal and regulatory policy part, which Melissa Campel Guru was recently named to head up.

There are five offices in this part of the division, the Office of International Corporation Finance, the Office of Mergers and Acquisitions, the

Office of Structure Finance, and most importantly I think to your work today, the Office of Small Business Policy and here in the room with me is our head of Office of Small Business Policy.

Raise your hand, Jennifer. Be proud.

She heads up our office. We also have an office of rulemaking. Jennifer's office does phenomenal work with small businesses.

So, they provide the guidance externally and within the commission on our offering adjunctions. Reg E, Reg A, Reg Crowdfunding, interstate offerings, et cetera, as well as on our smaller reporting company SRC rules.

They provide the expertise on all our rulemaking and policy decisions that impact small businesses. They have both a phone number on our website as well as an online form, and they respond to approximately 1,000 requests for guidance and interpretive questions every year.

So, that is an unheralded thing that our division does. It's not just rulemaking, it's not just the disclosure review program, it's that kind of frontline in-the-weeds work that I think we really need to celebrate and to cast a spotlight on.

That's incredibly important for entrepreneurs and our public engagement.

Public engagement and outreach is a huge part of my emphasis as director as well as that of my predecessor Rene Jones. We are making a huge effort now that the -- there's more in-person meetings to get out around the country, to hold ourselves accountable as public officials, to be transparent about what we do, as well as to get feedback on our rules and our operations within the division.

Specifically, we are casting a much wider net to speak to groups that aren't typically involved or aware of the SEC's role or federal securities law or generally.

We are trying to speak to groups in particular in underserved parts of the country, and we are starting this week on Sunday, Jennifer, my policy counsel Jeb Burn and I will be flying to Knoxville, Tennessee, and on Monday we will be making a presentation, multiple presentations at the University of Tennessee.

So, we are making -- we are starting our roadshow with Appalachia and really trying to get out the word to small businesses and investors on how our federal securities laws operate.

We hope to expand the roadshow to -- where I normally live in the West, to Indian country as well later next year. And I think that this will build on the very valuable work that the Office of the Small Business Advocate, the Office of the Investor Advocate, and the Office of Investor Education already are doing in terms of outreach around the country.

So, if you have ideas for how we can better do that outreach, how we can take that roadshow on the road, I'm all ears. We're very much about getting the word out.

I want to talk a little bit about some of the rulemaking items that are on the Reg Flex agenda that are relevant to your work today.

In rulemaking, we always take into account impacts on small issuers. We are always mindful of how to best promote capital formation and to reduce compliance costs for smaller reporting companies while maintain investor protections.

We are statutorily mandated under the Regulatory Flexibility Act to provide an initial analysis in any proposed rule that is subject to public comment. As well as a final analysis in the release considers comments received on the Regulatory Flexibility Act.

It is incredibly important that we hear from smaller companies, their advisors, and their investors, in that comment process. We are looking for data on costs and impact, and I can tell you firsthand, we look very, very carefully at those comments and weigh them very, very carefully as we consider recommendations to the commission.

It is a longstanding practice of the division to look at ways to have scaled disclosure and other accommodations for smaller reporting companies.

Here's some recent examples. In our performance rule which coincidently, Jennifer and Jeb took the lead on. I love watching Jennifer blush. For those of you who are watching remotely, I just love watching my staff soak up the adulation. It's like one of the truly sadistic things I get to do as director.

In the -- performance rule, we did recommend and the commission adopted significantly less disclosure requirements for smaller reporting companies. There was no peer group to shareholder return requirement, no requirement for companies selected measure, and less requirement for a tabular list.

We also had later recommendations that the commission voted to approve on our insider trading arrangement, the 10b5-1 rule and related disclosures.

And I have one of my former -- other former rule makers, John Fieldstone, who's also in the room, so

I'll make him blush a little bit too. Thank you for your work on the rules as well, John.

Still on our Reg Flex agenda are a number of other rules, which I'll talk about in a minute, but for now, I just want to note that we have the commission prior has made available several exemptions that were expanded in the 2020 Harmonization Rule release in Reg D, 506b and 506c, as well as Rule 504 where the offering limit was raised by 10 million in 2020.

In 2020, we also liberalized the Reg A exemption with new offering limits of 75 million up from 50 million.

We also have Regulation Crowdfunding where the offering limit was raised to five million up from 1.07 million. We are continuing to be interested in the impacts of the 2020 Harmonization Release and we encourage comment on any rulemaking that comes out of the division.

This is good not only for our obligations under the Administrative Procedures Act, it's good in terms of getting good policy recommendations up to the commission.

Like I mentioned, we have a number of rules on the Reg Flex spring agenda that may be of particular interest to this committee and on which we would appreciate even advanced feedback now as well as comment if and when a rulemaking does come out.

So, those would include the Rule 144 Holding Period, Reg D, and Form D improvements and revisions to the definition of securities held in record.

I want to thank the committee again as you provide input through your work here today. I want to thank the new leadership of the committee. It is an incredibly important task.

To my outreach point earlier, it's crucial we hear from small businesses when making policy decisions. It's really important that we get your input.

We would particularly be interested in feedback as we conduct our Quadrennial Accredited Investor Review. Any views you have on offering exemptions, including Reg A, and any other ways that we could have data-driven ways to review the effect of transaction exemptions. So, thank you very much.

MS. DUIGNAN: Thank you, Erik, and if time permits, would you be willing to take questions from the committee?

MR. GERDING: I will be happy to.

MS. DUIGNAN: Wonderful. Do we have questions for the director of the Division of Corporation Finance?

MR. GERDING: I'm a law professor. I'll call on you, cold call.

PARTICIPANT: What changes are you considering to the 144 filing procedures?

MR. GERDING: So, I can't comment on exactly what the Rule 144 rule might look like. I think, as you know, there was a Rule 144 proposal from several years ago.

If you have views on the way that that proposal was structured, that might be particularly helpful as we focus on our recommendations going forward.

We did have some changes on Rule 144 as part of our electronic filing release, which happened in 2021, which is trying to move a lot of the Rule 144 filings to electronic rather than paper.

Earlier in the winter, we also extended the deadline for filing of 144 forms back five hours in order to accommodate 144 filers. So, we've done some things or at either is one proposal out there already. We've done some work on electronic filings, but we're open for feedback on what you might be looking for.

MR. SUGINO: You mentioned the outreach you're doing in Tennessee. Can you tell me what sort of groups you're most interested in, and those are numbers that you're interested in as well to your outreach?

MR. GERDING: I think the groups we're focusing on in Tennessee are starting with small business owners, right?

So, entrepreneurs and entrepreneurs of in very, very different sectors. This might be startup company entrepreneurs that like, are more hopeful for getting VC funding.

But as well as your small businesses that, you know, are not looking to access VC funding, but are looking for other means of accessing capital. We're also going to be talking to investors including smaller investors and angel investors in these communities.

And then one particular focus that I have is also at trying to build capacity among advisors, particularly in regions of the country that I don't typically see in the conference circuit.

And to build capacity to get the word out among securities lawyers as well as audit firms, we're talking not only to lawyers in these communities, but we're also talking to law schools.

There's a lot of transactional components out there. The University of Tennessee has a very fine transactional program and that's in part not just to have immediate capacity and immediate advice to companies, but really to build a bench in terms of ensuring that the next generation of lawyers -- and I know this is important to folks like Stacey -- to make sure that the next generation is also providing solid advice, not just to firms and companies on the northeast corridor and in California, but all throughout the country.

If you have suggestions, Dennis and who else, we ought to talk to, I'm all ears.

PARTICIPANT: Will you be coming to L.A. anytime soon?

MR. GERDING: We should talk offline. I'd love to go out to L.A.

PARTICIPANT: Thank you.

MS. DUIGNAN: I'd love to get an understanding of how your office might be using technology to increase the efficiency and reduce the costs of compliance.

MR. GERDING: So, we have a number of technology initiatives that we are working very hard on. And that's critical as we try to do more with less. The personnel at the division, even though we've done quite a bit of hiring this year, we will still be under our 2016 staffing levels, and I think we're one of the few parts of the commission that will still be under 2016 staffing levels.

At the same time, we've had an IPO surge.

We've had a STAT surge. So, we have more public companies to review. So, we're going to have to get better at doing reviews that satisfy our statutory mission with the same number of people, or fewer people than we had in 2016.

And part of that is investing in technology so that we are really data driven in terms of figuring out where we think the most benefit for our statutory mission where the most compliance benefit, where the most disclosure benefit would be for any particular public company filings.

This is important, not just in our public filing space, but also in our Reg A space. So, Jennifer's group as well as our disclosure review program also looks at the Reg A qualification filings. And there too we have to do more with less.

And one of the things that we could particularly use feedback on is how we focus our resources in the Reg A space. Are there particular things that we should be looking for in Reg A filings to really again focus on our core statutory mission. There's -- it's an important exemption. It's very useful for businesses, and we want to be fairly targeted and smart in the way that we focus our common process.

MS. DUIGNAN: Okay. I guess it looks like we're done with questions. Okay, thank you so much. We really appreciate the insight and to learn more about your needs and how we can be helpful and what you're working on. So, thank you.

MR. GERDING: Well, thank you for having me, and please, you know how to reach me. So, please reach out if you have ideas for what we could be doing differently or if you'd like to talk about our roadshow and I'll volunteer Jeb to help coordinate that. So, thank you all.

Panel Discussion One

MS. DUIGNAN: Wonderful. Well, this has been an exciting morning already, and we are very much looking forward to digging into some of the proposed agenda items. So, we're going to start off with the question who out there is investing in funds that support early-stage companies and are there ways to encourage more investment into these companies?

As investors, we've definitely noticed a startling trend that has likely had an adverse effect on the optimal growth of the U.S. economy. There's been an undeniable lack of access of startup and venture capital for BIPOC and female founders.

Each year less than two percent of total venture capital dollars go to female founders and less than one percent goes to BIPOC founders. In thinking about how to get more capital flowing to female founded and minority founded businesses, it's important for us to understand how capital currently flows from the endowments, retirement savings, and insurance policies of working people to founders who can help actually grow that capital.

Large institutional investors, such as pension funds and endowments, tend to be extremely risk averse for good reason. And because they manage billions of dollars they often need to deploy tens of millions at a time to officially manage a portfolio. Therefore, they tend to prefer to invest in very large funds that also have very long track records. However, in order to increase diversity amongst venture capital asset managers, we know that smaller, newer funds need to be formed. Funds that are also more likely to invest in female and minority founders because those funds managers and the checkwriters within include females and minorities.

So, we raise this topic to discuss how to address the challenges and consider how to best encourage change in the right direction. What can be done to increase the willingness of capital allocators in making commitments to newer, smaller funds in order to increase diversity in the venture capital and asset manager community?

Might there be incentive structures or partnerships to develop and champion to reduce the perceived risk of investment in smaller funds so that there is a larger pool of capital flowing to these underrepresented founders.

So, to provide some context on the landscape, we have two folks joining us to speak today to share their perspectives with us. Our first speaker is Kwesi Quaye, partner at Fairview Capital Partners and a member of Fairview's investment committee. Kwesi is based in West Hartford, Connecticut, and focuses on research, deal sourcing, investment monitoring, and business development for Fairview's venture capital and private equity partnership and direct co-investment portfolios. Prior to joining Fairview in 2017, Kwesi was an investment officer at the Cook County Pension Fund. He also spent time with Price Waterhouse Coopers performing inside mergers and acquisitions and with Ernst and Young in the insurance practice where he led audit engagements.

Kwesi, we are so pleased to invite you to share your thoughts with us this morning.

MR. QUAYE: Great. Thank you, Erica. Thank you to the committee and thank you to the commissioners for allowing me to share our experiences and market insights on investing in diverse and emergent managers.

I'll use a presentation to kind of guide the conversation. Can everybody see my screen?

MS. DUIGNAN: Yes.

MR. QUAYE: Great. Okay. So, for an agenda, I just want to spend maybe a few minutes on Fairview Capital, who we are, what we do. I'll also go into the market overview of one minority owned venture capital and private equity firms. And then I'll talk about institutional investors and emergent managers and draw some conclusions based on, you know, what's been presented today.

And so, Fairview Capital was founded in 1994 and for context, we are the largest, arguably the largest minority owned venture capital and private equity fund of funds in the country. We are SEC registered, and we manage about $10.5 billion of assets in aggregate fund capitalization since inception.

We're focused on delivering strong risk adjusted private market returns. We're specialists. We approach investing through a variety of ways including access, market intelligence, decision making and nimbleness, and we're deeply imbedded, you know, in the private markets. And we strive to be true partners to sophisticated institutional investors.

Our business is threefold. We invest in diverse and emerging managers. We've done that for nearly 30 years. We also invest in venture capital funds, and on occasion, we co-invest in companies alongside the fund managers that we invested through our diverse and emerging manager program as well as our venture capital programs.

And is it relates to diverse manager and emerging manager investments, specifically, we really see ourselves as an innovator in catalyzing the next generation manager investing in the private markets. It's a difficult market to navigate successfully, we believe that we will succeed in implementing strategies that have generated strong performance for our institutional investors.

And we believe Fairview is one of the strongest brands and reputations in this space, which is significant advantage. And as I mentioned we've been doing this for 28 years. We've done this on behalf of 29 institutional clients. We've backed over 110 emerging manager funds, and we've backed over 40 first time funds. So, we've again, been doing this for a very long time.

And now I'll kind segue into just the market as a whole. You know, we believe that we have a strong commitment to knowledge sharing and insights. And the diverse and emerging manager market is opaque.

There's not a whole lot of data around who's raising what, but because we've been doing this for nearly 30 years, we've amassed an amazing database of who are the best managers. We've amassed a database of, you know, who are the managers investing in venture capital, who are the managers that are going out and really investing in the next generation, you know, of companies.

We've really served as a valuable tool for our stakeholders, including limited partners, general partners, and investment professionals.

And now I'll get into, you know, our data. Specifically, what we've done is we've externally published our market review of women and minority owned private equity and venture capital firms annually since 2014. We've been actively investing with diverse managers in partnership with many of the nation's leading institutional investors for nearly 30 years.

And as a leader in the category, we aspire to see every institutional quality women and minority owned firms in the market each year. And as a result, we've built the most comprehensive database of diverse managers in the country.

This has largely been developed through the team's network over several years through interactions with meetings, calls, industry conferences, referrals, affinity groups, inbound inquiries from diverse managers who know our strong reputation in the marketplace, and proactive outbound research.

Our data specifically reflects one of the strictest definitions of a diverse manager, that is, we only consider institutional quality private equity and venture capital firms that are greater than 50 percent owned by women or minorities at the management company level. That's what this data represents.

The firms must also be based in and primarily investing in the United States. In this year's midyear report covers firms actively raising capital through the first half of 2023. Which of course represents the current opportunity set for investors seeking to invest with diverse funds.

We've broken out the data across several dimensions, including fund sequence, fund size, fund strategy, and firm demographics to understand trends in the diverse manager market. So, let's get into the data.

So, at the highest level, the universe of women and minority owned firms continues to grow. It's worth noting that when we started externally publishing this data back in 2014, there were just over 100 women and minority owned firms in the industry.

Through the first half of this year, we're tracking approximately 831 firms meaning the universe has grown approximately seven times in size in just eight years. So, you can clearly see that the opportunity set is robust. It's growing at a 27 percent compound annual growth rate. So, there's a lot of opportunity out there.

Through midyear, new firm formation remains robust. One of the things that we're always looking for is when a new firm is raising a first-time fund, that's indicative of a new firm that could essentially become a long last and sustainable franchise where they can add talent and prosecute strategies over a sustainable period of time.

So, we marvel at fund ones because that's the indicator of new firms and the opportunity set of the industry growing.

And when we annualize the media results for this year, new firm formation is now based to exceed the record set over the previous two years, and that's despite the market conditions that we face today. It's important to note that launching a new firm is a significant endeavor. It can have a long (audio interference) between the ideation and launch bases.

So, it'll be interesting to see how the opportune set plays out during the balance of the year. But based on the historical trends, and even through the numbers that we've seen, you know, through the third quarter so far, things look to be pretty good.

A question that we often get asked at Fairview is what is driving the growth in the universe of women and minority owned firms. We think that there's four main reasons. For one, there's increasingly more diverse talent in the industry. This year we continued to observe increase in diverse talent entering the industry with operating and investing background and angel investing.

Second, many diverse professional (audio interference) from limited career enhancement. This has led some to build the conviction to start their own firm. Our observations confirm limited career advancement continues to be a challenge which could bode well for new firm formation.

Third, diverse managers are invigorated to develop a new firm with an inclusive first culture.

Diverse managers are reshaping the industry grounded in the knowledge that cultures that truly embrace diversity equity and inclusion can outperform.

We think organizations that have embraced inclusion are advantaged because they're able to recruit diverse talent and they're building strong brands with this philosophy. We've also observed this is a unique way of connecting with LPs, GPs, and founders who share similar values.

And then lastly, advice, mentorship, and other knowledge-sharing platforms are increasingly accessible for firm building. Our observations confirm that support systems remain robust and general partners are collaborating more than ever.

And now we're going to look at some of the breakouts, as I mentioned earlier. We're going to look at some of the trends in terms of fund sequence, fund size, and then some other demographic breakouts. So, beginning with fund sequence, you can see that all told, there are about 325 women and minority owned firms in the market this year, right now. So, they're out there. The opportunity set is very large.

Continuing recent trends, diverse managers represent newer firms, are targeted in smaller fund sizes and are primarily focused on venture capital strategies. In the first half of 2023, first time funds sponsored by women and minority owned firms represented 52 firms of the market -- 52 percent of the firms in the market, which is actually the lowest proportion since 2017.

We think this is a silver lining because that means that 48 percent of diverse managers are raising a successor fund, which is a fund two or higher and they're presumably building their franchises.

From a fund size perspective, the universe is targeted $100 million target, and then from a fund strategy perspective, about 76 percent are raising a venture capital fund.

Digging into the fund sizes, you'll see that, as I mentioned, the median fund size for a woman and minority owned firm is about $100 million, which compares to $300 million against the broader industries a fund three times the size of a typical diverse manager.

Limited partners, you know, we believe may be inclined to invest in larger funds sponsored by established firms, which could be a headwind for diverse managers who may be overlooked. In some cases, diverse managers do not meet minimum sized parameters implemented by institutional investors and -- including for many emerging manager programs.

The opportunity set really to invest with diverse managers is in venture capital. We've been breaking out the data in terms of venture capital, growth equity, and buyout.

When we started externally publishing the data, interestingly, most diverse managers were raising a buyout fund back in 2014. That landscape has shifted over the years. Venture capital, as indicated by the green line there, continues to be an outsized proportion of the strategies raised by diverse managers. That has come at the expense of buyout strategies, growth equity strategies, and other strategies. So today, 76 percent of women and minority owned firms were raising a venture capital fund.

Venture capital funds can be more challenging to evaluate. There are higher dispersions of returns in the category. Various entry are higher in growth equity and buyout which is why we believe there's been more firm formation in venture capital. And when we look at what strategies diverse managers are pursuing, technology, infrastructure, and special situations are their areas of focus.

Now, I want to get into some of the demographic trends, you know, that we observe. And now, beginning with African Americans, we know a significant majority were raising first time funds. African Americans were targeting medium fund size of $75 million which is up from $65 million in the prior year.

And so, our data reflects that there were about 127 African American firms in the market this year. That's a four percent increase compared to 2022.

When we look at Latinx firms, Latinx firms are severely underrepresented, but our data confirms that they're often raising a subsequent fund. And so, they represent about 11 percent of the total women and minority owned firms in the market. 49 percent of Latinx firms are raising essentially a Fund 2 or higher, and you'll see that the median fund size for Latinx firms is $125 million, which was actually up compared to $100 million in the prior year.

When we look at Asian Americans, most were in market with a successor venture capital fund. And then further, 80 percent of Asian American firms in the market were (audio interference) highest of the profile demographics.

And then in terms of median fund targets, they're also raised (audio interference). This is important to note because although they are raising successor funds, which would imply a step up in fund sizes, Asian Americans are still targeting a fund size in line with other underrepresented demographics.

When we look at, you know, women entrepreneurs, a lot of nuances when we look at different ethnicities within various women. So, to begin with, women-owned firms are often raising small early stage venture capital funds while African American women and Latinas are often raising the smallest of funds. When we look at African American women in particular, 77 percent of African American women led firms were raising first-time funds. 84 percent were raising a venture capitalist fund.

In the target of $50 million median fund size, which is unchanged from the prior year, and it's below, well below, the industry average. When we look at Asian American women owned firms, 93 percent were raising a venture capital fund, and most were raising a successor fund. Latina owned firms, again, very underrepresented. 30 percent were raising a first-time fund, and our data confirms all Latina owned firms were raising a VC fund. And the median target fund size is $45 million which is just the lowest of all the demographics that we've profiled.

And lastly, when we look at nonminority women, 78 percent were pursuing a venture capital strategy. Most were raising a successor fund, and they were targeted at $75 million median fund size. So, there's some interesting statistics to be shared.

But at the highest level, diverse and emerging managers are typically raising a newer fund, typically raising a first-time fund, typically raising a fund size of about $100 million, and they're typically raising a venture capital fund. And that is really the opportunity set. It's in venture. They're typically raising smaller funds, and they're typically raising newer funds.

We have some slides as to what this means for fund managers and limited partners. And this is against the backdrop of the market environment that we're in today, which is a little different than it has been over the last few years.

And so, key considerations for some general partners, those fund managers out there that are listening. You know, again, market cycles tend to have outside impact on institutional investor interest and capacity for emerging managers, particularly diverse and emerging managers. Emerging manager programs which are often critical sources of capital may not be as active and new programs are less likely to be launched in the near term.

You know, at Fairview we believe competition for capital will continue to increase and fundraising cycles may take longer than in prior periods. And we also believe that the importance of community has increased significantly. Advocacy and education remain important as does the sharing of best practices and having a collective mindset.

You know, for our limited partners, the opportunity to invest with the risk managers still remains significant and continues to grow. Presented some data earlier about just the market opportunity just continue to grow at a 27 percent compound annual growth rate. So, the opportunity is still out there.

The vast majority of diverse managers are building new firms, they're raising smaller funds, and they're employing venture capital strategies. And given the profile most diverse managers, the dispersion of returns will remain high meaning market coverage and manager selection will remain critical.

At Fairview we believe a programmatic long term approach has sent deployment of capital and manager selection will continue to be important, not only to performance success but also to the continued success of the ecosystem.

And so, given all that, we've taken a historical approach as to what we've seen. Now, let's look at what we think, you know, as look what could happen in the near term. So, in the near term, you know, at Fairview we believe new firm formation will continue, but the rate may not be as linear.

You know, diverse managers with longstanding strong track records with access to existing LPs will be able to continue to scale their franchises successfully, despite market conditions. We continue to believe fund sizes are likely to remain smaller and we've seen evidence of that as we meet with our various prospective managers. Venture capital remains the most represented strategy for diverse managers because of the lower barriers to entry, the growing ecosystem and the increase in talent. And the opportunity set of institutional quality diverse managers will remain robust. It has remained robust. We've made a business of it for nearly 30 years. We remain that to be the core. We expect that to continue.

Now, I'd like to change gears and talk about institutional investors implementing an emergent manager program and just some things to be aware of on the LP side.

So, just to put a framework around it, asset allocators can invest in emerging VC funds in different ways. Asset allocators, and Erik had mentioned earlier, include public pension plan, endowment foundations, high net worth individuals. They can invest in venture funds directly or indirectly through intermediaries. And then those funds would in turn invest in companies, presumably early stage companies that's where the opportunities that for many of the diverse managers are.

Venture capital has historically been an asset class where emergent manager programs can be impactful. As I mentioned earlier, new small and diverse managers are underrepresented in the industry. Emerging managers -- and it's important to note that although they are emerging, in our experience, many emerging managers are experienced investors. They just happen to be starting a new firm replicating the same type of strategy that they had been doing at a tenured firm.

In investing with new, small, and diverse managers can result in superior performance. When implementing an emergent manager program, you know, the guidelines can be designed to ensure that a portfolio can keep its risk adjusted objectives.

Investment programs may vary in size and sophistication, diversification, risk tolerances, and return expectations. And to this day, there's really no industry-wide standard definition for emerging managers, rather most institutional investors develop their own specific definition for emerging managers based on their requirements.

We believe there's many benefits to investing in emerging managers. To begin with, there's just motivation. You know, managers who are launching a new firm are likely to be more energized and motivated than more established firms. When you've started a firm, you've invested lot of sweat equity, you've invested a lot of capital. You're going to be more motivated than perhaps, you know, a more established firm that's raised, you know, many fines, many dollars, and has grown so much that you -- it's increasingly become a smaller proportion of the firm's growth.

Differentiation would be the next point I would make. Newer firms may feature different networks, relationships, and approaches than established firms. So, many emergent firms have differentiated net worth, different FA groups. They may have different relationships that lend itself to newer opportunities which is a competitive advantage.

You know, emergent manager firms feature smaller teams and collegial environments. We believe that this allows an emergent manager to be nimble in its reaction to opportunities and market changes.

And then strategy fit. Certain strategies may just be best suited for emergent managers. From a performance perspective we believe these characteristics play out and can be creative to institutional investor portfolios.

And then lastly, and it’s not something that's talked about very often, but it's really important. It's access. I think, you know, one of the things that is not really talked about is the best firms don't need your money, quite frankly. And emerging managers are a great way to get access to the best firms so that when the successful ones ultimately raise larger funds, typically what happens is there is more LP demand than what can satisfy the GP's fund size. So, when you're able to invest in an emergent manager early and grow with the firm, it allows institutional investors to have preferred access to subsequent funds. And that is a tailwind for performance.

So, once an emergent manager definition and strategy's in place, an institutional investor must decide how to really best implement the program. Implementation of a program can be done really in two ways. It can be done internally or an institutional investor can utilize an investment management firm.

So, internally, you know, an internal approach has worked for some institutional investors, but there's some caveats, you know, in our experience. Those that have done it well in house were serious about emerging manager programs. They made a long-term commitment with a high level of consistency and methodology and personnel.

So, as an example, if an institutional investor was to invest in Fund 1, and kind of be done, it's not really enough, you know. The first fund, you know, is a catalyst really for the subsequent fund, but it's just as important for the institutional investor to be there for the subsequent fund as it is for the first fund.

And then the other option these investors can do is utilize an investment management firm. You know, many institutional investors choose to utilize an investment management firm because emerging manager programs can be considered relatively niche. You know, some investors just may not have the in house resources and expertise required to effectively implement the program.

And we know there's benefits to utilizing an external investment manager. You know, this is in the areas of customization. You know, investment managers typically can develop customized separate accounts, you know, just experience, an investment manager with experience implementing emergent manager growth can add significant value at the cost, you know, the fees associated with hiring an investment manager to implement emergent manager program are generally negotiable.

From an access perspective, you know, if the investment size for an emerging manager does not comport with the restrictions of the investor, then the investment manager may be optimal.

And then education, you know, an investment manager can help educate institutional investors and emerging managers and then there's resources. Tracking all of these emerging manager funds that come to market is extremely time-consuming, deep due diligence, expertise, and insights. And so in that case, it might be better to just partner with an investment manager.

And now, I'll get to the conclusion. The truth is, emerging managers can help institutional investors achieve their objective. Emerging managers may be easily overlooked in a broader, private equity portfolio, but no matter what approach is taken, it must be thoughtful and deliberate.

A sound emerging manager program can provide many benefits and should be able to address the unique challenges and potential pitfalls that accompany the opportunity of investing with emerging managers. And if executed well, an emerging manager program can pay significant dividends in the form of returns and diversification.

Thank you, and those are my prepared remarks.

MS. DUIGNAN: Thank you, Kwesi. That was so informative, and we really appreciate your time and thoughtfulness to prepare this for us today. I'd love to open it up to questions from the committee.

PARTICIPANT: Thanks. Thanks very much for the presentation. I'm curious, your thoughts you referenced that a lot of these emerging funds, minority, BIPOC, they specialize in the venture capital arena and I'm wondering, like, what is the impact to the fund, but then also how might that impact the small businesses that are looking for those emerging funds to invest in them?

MR. QUAYE: Sure. Thank you for the question. So, at the highest level, venture capital truly is the first line of defense in terms of innovation and company creation. And so, when you're looking at entrepreneurs that are looking to start their businesses, one of the things that we observed is relative to perhaps other founders, most entrepreneurs don't have access to that friends and family wealth.

And venture capital can be a nice segue to provide that gap. And so, one of the things that we've seen play out in the market place is although many emerging managers are often raising, you know, smaller funds, that also means that many emerging managers are investing earlier. So, when you look at the venture landscape you can invest from the pre-seed, which is just ideation, you could invest in the C round, the Series A round and of course, these companies become more mature later on, but one of the things that I think venture capital has really done, particularly for diverse and emerging managers is when you look at diverse managers as a whole that are focused on venture capital strategies, they're able to invest in companies earlier. And when you look at entrepreneurs that may be BIPOC in particular, having access to that capital earlier on is helpful. And so, that would probably be my response to that.

MS. DUIGNAN: Jasmin and then Sue.

MS. SETHI: So, when we're thinking about the allocator and the pension plans and endowments and so forth that are building these emerging manager programs, I'm interested to know your perspective on how do we think -- or how do they think about the diversity angle in particular as it relates to investment?

And the context for this question is, you know, there are some who would argue that the diversity component is not necessarily material to investment, that it has value, and that the other components, you know, when you look at the strategy, the risk, the performance to the extent you have any performance history and so forth, are the metrics and, you know, where does diversity fit into that?

How would -- what would be your response and what are the allocators thinking and saying, no, this is actually important for our investment decision?

MR. QUAYE: Yeah, thank you for that question. I would broad stroke it and say institutional investors look at diversity differently, of course. But I think what's very clear is that diversity leads to superior performance.

I think you have to have that philosophy up front, and at Fairview we do, and that's always been our position, you know, to institutional investors. So, institutional investors that see diversity as an enablement to achieving a portfolio's objectives, I think that's where there's really no ambiguity. It just makes perfect sense, right.

I think in instances where diversity is seen as somewhat concessionary to, you know, meeting the portfolio's objectives, whether it's some kind of carveout within a broader portfolio because we feel like we need to do, you know, size by some other mandate. I think that's where it gets a little difficult for institutional investors.

So, I think it's really those institutional investors that see diversity as a creative to their portfolios, that's really the best way to then implement, you know, those types of diversity initiatives. I will say, and I'm drawing on prior experiences, one of the things that I observed well is you have to be able to measure it some type of way. And you know, for many pension plans out there, many of them are very highly regulated and, you know, they have various statutory limitations and guidelines and investment policies, but those that have essentially adopted it into their investment policy, it's certainly much easier to measure and have it be a firm philosophy. So, that's what I would say to that question.

MS. DUIGNAN: Sue?

MS. WASHER: Yes, thank you, Kwesi. I think the information you've provided was very, very informative, and certainly I had not heard of your annual report before, and I absolutely will have that on my radar now to be able to review. And one question I had, you mentioned that there are 325 active --

MR. QUAYE: Yes.

MS. WASHER: -- active, diverse funds. And I'm wondering if those funds are published in your report because I certainly think minority business owners having access to the list of minority-led firms would be an astounding step up, and I would doubt that many know who those 325 firms are. So, how can we address that?

MR. QUAYE: Yes. So, there are a number of trade organizations. I think that would probably be the best pitstop to address, you know, the entire universe, the names, who they all are. I can certainly look into that and provide that level of information at the appropriate time.

But broadly, most of them, you know, yeah, it does take some work. But I would say the infinity groups in particular, there are a couple that come where that would be the first pitstop, and they would be able to certainly share some of the names they'd be happy to engage at that time.

MS. DUIGNAN: Thank you. Well, we are looking for interesting data to link to from the office website,

so we'll keep looking for it.
PARTICIPANT: Eric, I had one question for --
MS. DUIGNAN: Yes, we are, I think we'd be able to take some more questions. But we did want to give one opportunity for the online folks, so Herb, we'd love to call on you.
MR. DRAYTON: Great. Thank you. Kwesi, thank you for a very solid presentation. I'm just going to give you all three of my questions and you can take them in however order you want. Now, one is your thoughts on the famous fund litigation that's currently outstanding. Two, your thoughts on -- are you saying emerging managers use placement age events as a part of their fund raise strategy? And the last one, what is the average amount -- average level of capital being deployed with the startup companies at this point by either VC firms?
MR. QUAYE: Okay. So, I'll address the fearless fund question first, and that's certainly something that we're following rapidly. And you know, it's actually disheartening that it's something that's even happening. When we look at Fairview, we actually -- the firm was founded because 29 years ago, the firm was not -- the industry was not inclusive. And investing in diverse and emerging managers, you know, it

just wasn't being done. So, you know, here we are 29 years later and there are, you know, challenges to creating a more inclusive environment. It's certainly something that we're monitoring and we'll continue to monitor.

The second part, I believe your question was around placement agents. I think everyone has different experiences using placement agents. I think when you're starting a firm for the first time, really your brand is yourself. And so, I think in our experience, you know, when you're building relationship it's about the founders and the general partners. So, if you're trying to build authentic relationships with institutional investors, I think it's a little harder to do with placement agents when you're at the firm formation stage.

I think placement agents can be -- can be helpful for some firms when, you know, perhaps you've raised prior funds, you have an established team, the practices and processes are largely defined.

The average capital deployed to startups, I don't have that data on hand, but we can do some back-of-the-envelope math. Diverse and emerging managers are raising, you know, typically $100 million per fund, and they're building diversified portfolios. Some are between, I don't know, 15, you know, north of 15 investments. If you do the math, you can kind of figure out essentially 300 funds in the market and how much would be largely deployed, based off the data that we see. So, of course, it's still small relative to the industry average, but that is what we see today.

MS. DUIGNAN: Vincent?

MR. CORDERO: Great presentation. I really appreciate the data. And then also, just quickly, congrats on your career, on your being a former Chicagoan, and on the incredible work that the firm has done for decades now. I'm glad to learn about it. If we wanted to follow up with you, what's the best way to connect with you?

MR. QUAYE: Yes. So, there's the whole team. It's not just me at Fairview. So, connect at Fairviewcapital.com please.

MR. CORDERO: Got it. Okay. Awesome. And then the question I had was, you know, something that we talked about in our first session, or at least my first session on the committee in June was myself being in the marketplace is really understanding the Latino marketplace as the most underrepresented under invested market.

Again, you see this across industries,

including in the venture market, both on the emerging fund manager side, but as well as on the, you know, founder seeking, particularly earlier stage investment.

Your data seems to very much affirm that, where Latinos and Latinas were the most under-invested group within the overall diverse category. That even becomes more dire as I shared last time when you take into account that Latinos represent 20 percent of the total U.S. population, 25 percent of the Gen Z or Millennial population in the U.S., and then from the annual report that was published from the SEC, in those seven or eight major marketplaces where most of the capital was both accumulated and deployed and we know those marketplaces across the country, Latinos for the most part represent either a plurality or majority of those populations in those markets of high capital deployment.

And yet, we have Latinos being the most underrepresented group from an investment standpoint having access to capital and networking key. What do you -- you know, in the work that you guys have done, I mean, I appreciate you flagging that because many times that's overlooked. What do you attribute that to? What do you guys look at that because again, as, you know, Erica talked about when she opened the remarks in the terms of -- and I appreciate Jasmine's question as well because it spoke to the same thing.

This is at the end of the day really about maximizing the economic potential of America and the world. And doing so by granting access to those who have been previously excluded from it, not having access to it. And you know, that's kind of good for everybody, good for America and good for the world because we all benefit from that.

As you guys look at this with your firm's, you know, reputation and history and expertise in this, what do you attribute that to particularly, again, with this challenge with Latinos having access and being the most under-invested, and what do you guys look to in terms of, you know, as you looked at your conclusion points? You know, we look forward for this committee or others who are interested, what are things that we need to do and focus on to turn that around?

MR. QUAYE: Thank you for that question and your comments. I really appreciate it. I think first of all we just have to continue to put a spotlight on the underrepresentation of Latinos. It's something that we've seen year after year.

And from my prior experiences, you know, across asset classes that was the case too. It's certainly something I don't think we have a clear-cut answer as to why it's been that way. We have seen very small incremental gains in terms of new firm formation relative to Latinos, but it still lags relative to other demographics, you know, in particular.

I would say there's probably one thing I would offer up would probably just more support systems, more affinity groups. You know, there are a number of other affinity groups that I think, you know, for African Americans, Asian Americans, you know, women in particular as well.

There's just more organizations that are putting on more conferences, more events, more networking activities. So, maybe more of those, you know, in the Latino community, and there's a few organizations that come to mind, but there could be more, I think. I think that would go a long way, but I think first and foremost, we all need to kind of get on the same page and really recognize this underrepresentation and really make it, you know, something that needs to be addressed head on.

MR. CORDERO: Look for a note from Vincent Cordero, I'll be sending you a note.

MS. DUIGNAN: Thank you. Diego?

MR MARISCAL: First of all, thank you again for the presentation. I thought it was very insightful. So, just for a bit of context, so, I work on supporting founders with disabilities specifically, and I think, you know, as many mentioned, there's certainly underrepresented support for underrepresented founders, but curious from a data standpoint, you know, when you look at the -- you talked a bit about definitions and the lack of standardization.

So, just curious, when you're looking at your own data, you know, how do you define diverse fund managers from a data collection standpoint and then, you know, have you considered disability status as part of that definition. And if not, you know, what steps could help you get there?

MR. QUAYE: Sure. So, the data that we shared from a market insight's perspective considers all the demographics I had spoken about, African Americans, Asian Americans, women.

And then the second question as it relates to disabilities, we track also veteran disabled managers as well. It's not included in this report, but we do track that as well, and it's certainly something that we'll continue to build on as we build out our database.

MR. MARISCAL: So, just as a follow-up, so then that data is part of the report, the annual report that you do --

MR. QUAYE: It is not -- it is not included in this report. It is not.

MR. MARISCAL: Oh, okay.

MS. DUIGNAN: Bart?

MR. DILLASHAW: So, I've just got a question. When you're talking with institutional investors that have expressed a desire to get, you know, exposure into emerging markets, are the challenges that they face related to access to the right sets of data with which to evaluate emerging managers or are there other barriers, for example, regulatory that might be, you know, relevant to the SEC to think about?

MR. QUAYE: Yeah. Thank you for the question. I would say it's probably more of a -- there's probably more screening restrictions.

So, I shared a lot of data around the profile of most diverse and emerging managers, and I had mentioned that, you know, most are raising, you know, a first-time fund. Many are raising a first-time fund. Many are raising a fund size of $100 million and many are raising a venture capital fund.

And I think when you look at, you know, primarily some of the larger institutional investors that are looking to invest, they're looking to invest substantial amounts of money, and when you look at how much an institutional investor is looking to invest versus the fund size of many of the funds that are being raised by the (audio interference) there's an over-representation from the LP to absorb too much of what would be satisfied in the fund.

So, for example, if an institutional investor was to deploy, say, $100 million, $100 million cannot be absorbed by that fund that's raising $100 million. There needs to be risk mitigation and diversification. There needs to be other investors in the fund. Most institutional investors don't want to be more than a certain percentage of the fund, typically ten percent is a number that comes to mind.

And so, I think the challenges for those institutional investors that are looking to invest, endorsing emerging managers, it's hard to put the money to work because the fund sizes when you factor in the diversification and the risk parameters that the institutional investor has typically set out in their own portfolio and construction models makes it challenging to do that.

So, that's one point I would make. I think some institutional investors, you know, some don't invest in first-time funds. Evaluating first-time funds can be difficult. You have to look at the track records prior to where, you know, the team is historically invested and you know, for some institutional investors some don't invest in first-time funds.

So, if you don't invest in first-time funds, you've essentially excluded a large part of the opportunity set of emerging managers. Because as we mentioned earlier, first-time funds are a substantial component of emergent managers raising capital today.

You know, the fund size, some institutional investors look at, you know, certain fund sizes and there are minimums in some cases, and you know, $100 million is typically below the fund size that many institutional investors look at. So, that's a challenge and then, you know, venture is a challenge sometimes as well.

When you get some institutional investors, some are able to take more or less liquidity, venture is, you know, an illiquid asset classes as are other alternative investments, but essentially, if you have an institutional investor that does not invest in venture, that does not invest in newer funds, and does not invest in fund sizes that are, you know, $500 million, I think that's really where the challenge comes to play and why institutional investors are having difficulty allocating to diverse emergent managers.

It's really the portfolio construction of the institutional investor and how that balances with the opportunity set of diverse managers. That's really what's been, I think, the biggest challenge, and that's before all the regulatory hurdles.

MS. DUIGNAN: Thank you, Kwesi. Marcia?

MS. DAWOOD: I'm curious as to where you have the cutoff. Is it just -- did you look at funds that only have institutional LPs. I'm coming from the angel world, and I know so many minority-led funds that are, you know, ten million, 25 million, very, you know, much lower. Were those included or was there a cutoff?

MR. QUAYE: They were included. They were included. In fact, a lot of the data are managers that, you know, they have angel investor track records. They are raising, you know, $25 to $50 million that is all in the data.

MS. DAWOOD: Thanks.

MS. DUIGNAN: I think one thing that's interesting too is when we say oh, we know people who have funds that are ten or 25 million. Very often when people say they have a fund of such size, but they actually have under management could be, you know, completely a mystery.

So, I think it's interesting. The one follow-up question I have for you, Kwesi, was on the limiting factor of the GP commit and how that might lead to smaller fund sizes for underrepresented managers.

MR. QUAYE: Hm, okay. So, that's a good point to make. So, just to kind of walk through the question a little bit more. So, you want to make sure that -- every fund wants to make sure there's proper alignment with the fund manager and the limited partners.

And when a fund is raised, the general partner, the manager of the fund, would need to put up what's called a general partner commit, which is usually a percentage of the fund and seeing, you know, commits in the range of .5 percent to 1 percent, and so, if you're raising a larger fund, actually needs to put more money up as part of the GP commit, and if you're just starting out raising your firm for the first time, maybe you've hired maybe one professional or two and you're building out your infrastructure to then put on, you know, a substantial GP commitment can be challenging.

So, it's certainly something that, you know, we continue to take solace in the fact that who are the people, you know, are they able to put up the GP commit, but by and large the GP commit has not really been a dealbreaker from our perspective. It's really been, you know, the track record, the team. For some institutional investors, it could be but yeah, that's what I would say to that question.

MS. DUIGNAN: Okay. Dennis?

MR. SUGINO: Question that I have is -- I understand you're the focus of your business model, but I'm a little still unclear about the strategy. Are you a -- do you take positions in the managers or are you a fund of funds or are you both?

MR. QUAYE: We are a fund of funds. We do not take positions in the managers.

MR. SUGINO: So, second question is, I'm curious as to the opportunity set going forward, as you would know better than I, a lot of venture positions among endowments and foundations and pension plans are over-allocated today because of the runup in the market and a lot of investors are focused on re-upping with existing managers. Do you see the opportunity set for new managers in this environment?

MR. QUAYE: I do. I do. Thank you for that question.

There's certainly been an incumbent bias, I think in the industry, particularly in periods like where there is perhaps macro-economic uncertainty and this perceived flights of quality where it's easier to just re-up with an existing manager rather than, you know, evaluate and do work and invest in a new manager.

You know, in our experience this is actually the best time to really, you know, identify the next generation of managers.

It's really during periods like this, and you know, in times like this, you just see a lot of market dislocations and you know, some of the tenured managers, larger managers, you know, they're always not as close to what's happening on the ground, and when I go back to what are the benefits of some of the emerging managers that I spoke about earlier.

It's the motivation, it's the access. Those play out across all time periods. So, we would expect that to be no different.

As it relates to institutional investor portfolios and asset allocations, obviously evaluations change quarter to quarter, year over year. We've always looked at venture capital as a long-term asset class.

I mean, the funds that institutional investors invest in, these are ten-year partnership terms, so yes, I think there are periods of time where they'll be unallocated, overallocated, institutional investors will probably rebalancing to meet their targets and, you know, at some point, it will all come back in line.

But again, venture capital has been, you know, really the lifeblood, you know, of the economy. It's a great source of wealth. It's a great source of innovation.

Many of the venture-backed companies, even through the pandemic, and during these challenging times, were really the companies that we needed most to get us through those tough times.

And whatever is happening, you know, in the future we would expect that venture capital to be a strong component of that.

MR. SUGINO: Last question, if I may. I used to advise estate funds when I was an investment consultant, and those funds, one in particular, has grown from 20 billion to over 100 billion, and if the fund sizes of these are 100 million percentage that it represents a portfolio, it's exceedingly small. So, unless you do a fund of funds, it's almost impossible to invest in --

MR. QUAYE: That is correct.

MS. DUIGNAN: Diego?

MR. MARISCAL: Yeah, so just as a follow-up question to my comments before, I was really kind of excited to hear about your comments regarding, you know, the need for standardization of how do we define what a diverse fund manager is, right?

And so, I’m curious as we think about, as a committee, sort of what are the actional steps that we could be taking, would you say that a recommendation on sort of how do we standardize what it means to be a diverse fund manager, would you say that that would be a useful sort of set of standards?

I presume the answer is yes, but I just want to hear more, you know, from your own thoughts and experiences. I presume it's a recommendation to standardize and perhaps a recommendation of what that standardization looks like would be really useful.

MR. QUAYE: That could be useful. I'm a little hesitant to put out exact guidelines or terms because, you know, the portfolios that we build are customized and I think one of the things you want to be mindful of is it's -- there are many institutional investors that have various stakeholders.

And in some cases, you know, the investment policies and the boards have their own investment objectives. So, you almost want to leave in some respects the ability to have flexibility so that institutional investors are not basically going against their own investment policies and guidelines and things like that.

So, I think there's probably more work to be done just around the largest institutional investors and how that kind of comports with, you know, the mission of the committee.

MR. SUGINO: So, just as a follow-up. So, I totally hear where you're coming from, and you know, the pressures of various investor communities, my fear would be -- and I'm curious to hear your perspective -- wouldn't then that -- wouldn't that mean that we're segmenting the data of what it means to be underrepresented fund manager or diverse fund manager because if we have different definitions, then it means that different segments are essentially measuring different things?

MR. QUAYE: Yeah. So, the data that we presented is in line with our portfolios, right? So, this is our proprietary data. This is (audio interference) proprietary data.

So, this is one source of data. I think there's many sources of data as to, you know, what the industry looks like from a one size and opportunities perspective, but when you look at the strictest, one of the strictest definitions of, you know, diverse managers, this is the data that we're prepared to share today.

MR. SUGINO: Got it. Thank you.

MS. DUIGNAN: Did you have a question? No? Okay. All right. Wonderful. Well, it looks like we've had some amazing questions from the committee. Kwesi, we want to thank you so much for your time and perspective on this truly important matter, as well as the three decades of work that Fairview has done to advance diversity in the investment sector. So, thank you so much.

MR. QUAYE: Thank you. Thank you to the committee. Thank you to the commissioners.

MS. DUIGNAN: Thank you. So, with that, I would love to see, given kind of the time and enthusiasm for our two speakers in the morning, that perhaps Bailey, we could do your session in the afternoon. Would that still work?

MS. DEVRIES: I apologize. But I can't be here this afternoon.

MS. DUIGNAN: Oh, you're not going to be here? Okay. All right. So, then let's maybe dive into some of your slides, if we can.

MS. DEVRIES: And I don't have slides today. So, I'll keep this conversational.

MS. DUIGNAN: Oh, okay. That's great. I did get some slides.

MS. DEVRIES: From my team --

MS. DUIGNAN: Yeah. So, that's why I was like, oh wow, she has a whole thing. So, maybe not. Okay. All right. Well, with that, we know the SBIC has done some amazing work this year to help solve some of these problems we're talking about. So, we are so pleased to have committee member, Bailey DeVries, here with us today to update us on the new innovations in the SBIC program for discussion. Thank you, Bailey.

MS. DEVRIES: Thank you, Erica. And I love that the slides will be available later, but if I may, I'd love just to have a conversation with everybody in the room. And I think it builds very nicely on the Fairview presentation and actually, as a nod to history for those that are not familiar. JoAnn Price, who was one of the founders of Fairview Capital, she was actually the head of the Industry Association of Minority SBIC Funds back in the day.

And that is the note of history of how Fairview was start is that she was leading that Industry Association and several of the members, the GPs and LPs said we need to figure out a pathway to raise more capital for these minority-led SBIC funds.

And with that, that community came together, and she was able to launch Fairview, and their initial strategy was investing in minority SBIC funds, and SBIC funds were the original venture capital funds in the U.S. for many that are not familiar with that. So, I think it's an interesting note on history and important to understand as you think about where we're going today.

So, for a little bit of background on the program overall, the SBIC program's office is to invest my company program was founded 65 years ago in the Eisenhower administration in response to a study that was launched by the Federal Reserve Board that found that while we have amazing capital markets in the U.S., there were gaps in terms of the flow of funds to small businesses, particularly small businesses that were involved in manufacturing, and creating products in the U.S., and businesses that were outside of major cities in rural areas.

And with that, they launched the SBIC program which was designed to help amplify our amazing capital markets that we have in the U.S. which are one of our biggest competitive advantages, and I say amplify, right?

So, it was about how can we align incentives and send demand signals and crowd more private capital into areas where the money is not flowing but it's not concessionary capital, right? This is return-seeking capital. But the equation needs to be adjusted in order for the duration of the investments to shift or for the return profile to shift relative to the risk associated with that return.

So, for 65 years, the program has been incredibly successful. It has gone through different iterations and at one point in time for many years we offered too what I'll call products on the shelf. So, two investment instruments. One was a debt instrument that we still have today.

It was called the debenture where we would give a loan to private funds, and that loan would have to be paid back to the SBA with semi-annual interest payments, but it was just a loan. So, we wouldn't participate in any of the profits, just principal and interest repayment.

And then we had another product called Participating Securities where we actually did participate in the returns. And through those two programs, we gave rise to many incredible funds across venture capital and private credit, buyout, some of the companies that were the amazing recipients of SBIC funding were companies like Apple Computer, Tesla, Intel, Whole Foods, lots of brand names you know, they were able to grow and -- well, to start, grow scale and go public in many situations because of initial funding that they received from an SBIC licensed fund. So, incredible, incredible history.

And what we have found over the last 20 years or so, gosh, going back even a little bit further following the introduction of the Federal Credit Reform Act, if anyone's familiar with the Federal Credit Reform Act, lots of federal loan programs. That legislation required any federal loan program to be considered a zero-subsidy program. So, what does that mean?

So, the program had to be no cost to taxpayers, so it had to be able to pay for itself, so the beauty of that is that Congress doesn't need to appropriate any funding.

So, no cost to taxpayers so long as we have a zero percent return and that's how even. With that, and coupled with the dotcom bubble bursting, there was a philosophical shift to focus on more banded return type funds and more private credit, mez debt, and some buyout.

The Participating Securities Program, which supported many of the venture funds was also sunset. There were flaws in the design of that program in legislation that could not be fixed through regulation.

It had a time-based return metric in there, IRR, and that doesn’t match with cash on cash investing and can be gamed. So, that program was sunset.

So, then we were left with one instrument. One instrument that worked really well for mez debt and buyout private credit. Program's been very successful. Okay, so things are working well.

Now, my annual interest payments. If you have a venture capital fund, if you have a growth equity fund, if you're doing a fund of funds, do you have cash being thrown off every six months to pay semiannual interest? No, you don't.

It doesn't work. It's for -- it's a mismatch of cash flows. And so, as a result, those types of investment strategies, if they wanted to get SBIC funding, wouldn't work. They'd default. Not because they were bad funds, not because they didn't have great returns, they just couldn't service the debt.

So, we asked ourselves, gosh, what can we do through regulations to fully meet the mission and intent of Congress if we haven't been able to support investments in early-stage funds because we know those funds lead to company creation and company growth.

And the mission and intent of Congress in the Small Business Investment Act states very clearly that we are to provide equity and long-term loans and debt funding to small businesses to help them start and to sustain and grow.

Gosh, we need another debt instrument, one that doesn't have semiannual interest payments required. Why don't we just draft off of things that we know work quite well in other areas of the fixed income market and let's have essentially an accrual bond where the interest accrues over the life of the instrument, but you can prepay whenever you have cash flow so that way you can manage your interest balance and pay off the rest at the end of the day.

And so, we did a lot of work to model that, test it out, and we are thrilled that on August 17th, we launched that into market. Not only did we launch that new instrument into market, but we took a step back and we said how do we create more flexibility in terms of our regulations, so that way we can be confident that we are not creating situations where there is concessionary capital but we know that we are aligned to the flow of capital in the private markets, you know, with the philosophy that capital will flow where it's easiest to go and it gives the highest return, let's try to align our regulatory framework and our standard operating procedures with what we know works well within private markets, so that way we can crowd more capital into funds that are well-positioned to invest in small businesses and startups.

And how do we meet some of these smaller funds and early-stage funds where they are? What can we do in terms of lowering barriers to participation in our program by thinking about costs associated with our application.

If you don't have management fees, it's -- you don't really want to spend a lot of money in applying for a federal loan program. So, how can we lower some of the costs there? But also, how can we think differently about how we partner with funds?

And what I mean by that is I said, okay, well, we've always just worked with direct funds. Why don't we work with fund to funds as well? Why work with fund to funds?

All of these issues that we just talked about, right? They have the ability to be checkwriters to smaller funds and given that fact, then they can accept more institutional capital that smaller funds cannot accept. They can also serve in a mentor capacity to those smaller funds and help them with building relationships, raising capital from other sources. And also learning more about our program if they did want to become standalone SBICs.

But we felt that this would be a way for us to increase the number of pipes into the ecosystem, so that way you have more GPs as asset allocators that are getting money from asset owners that can then have relationships with the small businesses and startups in their communities to broaden our reach and help us achieve the mission and intent of Congress around company creation and company growth and also job creation.

So, that's where we stand today. And we are accepting applications for our new instrument, which is the Accrual SBIC and the Re-investor SBIC which is the fund to funds license. So, we are -- we're really thrilled.

We also hold dear a principle of protect the core of what is working well. The program, like I said, has been operating at zero subsidy. We have to keep doing that in order to make sure that it functions well, and we can support more and thrilled to say that Congress increased our commitment ceiling last year from four billion to five billion, which provided another billion dollars in capacity for us to allocate to new managers and in the president's budget for Fiscal Year '25 we have that up to six billion with a 15 percent discretion to go higher, so that would be 6.9.

Last year, we committed 3.8, so it is nice to know that all of the existing program participants can rest assured that, you know, we're not taking from Peter to pay Paul, but we are certainly broadening out the diversification of investment strategies within the pool so we can finance more businesses.

I went through that quickly because I know we've had a long morning. But I'd love just to take a step back and answer any questions again -- will also be available afterward.

MS. DUIGNAN: Thank you so much, Bailey. That was wonderful. Diego?

MR. MARISCAL: Yeah. Hi, nice to meet you, Bailey. Great. So, yeah, my question is focused around, not surprisingly, folks with disabilities, but specifically, we were part of the Community Navigator Program. And that program, just for context for everybody, brings a number of organizations together to support underrepresented communities, gaining access to SBA resources, right?

And we saw a drastic, you know, engagement of the disability community, and different partners coming together, and a lot of small business centers saying we didn't know how to support founders with disabilities and this is a good way for us to learn, et cetera, et cetera.

So, just curious

MR. MARISCAL: Is there an opportunity to collaborate within your office. How are you thinking about the Community Navigator at large? Because I think one of the challenges that we're seeing is that it was a two-year program. We don't, you know, the future of it, it's still very uncertain.

So curious, is there a way perhaps continue some of that work that we saw, you know, through your office? How are you guys working together? Just want to get more color there.

MS. DEVRIES: No, it really is an excellent program and I just amazing that Congress had funded it and I remain optimistic and hopeful that they'll continue funding it.

So the program, that program is run through the Office of Entrepreneurial Development. I have just an incredible colleague, Mark Madrid, who leads that office. I lead the Office of Investment & Innovation.

So we have the SBIC Program, our Investment Program, and also a portfolio of federal innovation programs. The SBIR and STTR Programs, Small Innovation Research and Tech Transfers where we work with 11 agencies across the federal government on their R&D spending for grants and contracts for that earliest of innovation.

And then a series of grant and prize programs that are focused on innovation accelerators and business incubators. So the Growth Accelerator Fund Competition and regional innovation clusters.

I give that as context to say that some of those regional innovation clusters also have been recipients of Community Navigator Awards within the sphere of what I can influence and control, it's within, you know, that umbrella of our innovation ecosystem partners and they are -- they're not pilots.

They are well funded, which is fantastic and we do have a big commitment to be doing more education work with the SBDC's, as well, and trying to bring more resources to bear around our capital programs, beyond just the technical assistance that is provided.

So I think that you'll see more coordination across some of the technical assistance programs as we go forward to ensure that if there are any lapses of funding on one program, it doesn't mean that that history and those relationships are lost.

MR. MARISCAL: That's great. Just as a -- so with the Growth Accelerator Program would that fall under your purview? Okay. Got it. Got it.

I just ask because just for sort of context, so we also participated in that program and from a disability standpoint, saw some barriers, in terms of accessibility, in terms of clarity.

So we'd love to talk to you more afterward.

MS. DEVRIES: So good. I have an amazing woman in charge of that program. I'll make sure that she's getting --

MS. DUIGNAN: We'd love to invite Herbert from Webex for a question and after that we'll have time for one more question from Jasmine.

MR. DRAYTON: Thank you. Just a quick question. Is the link to apply for the new program already up on the site?

MS. DEVRIES: It is. It is. So if you go to the website, and I can follow up with this, and then it's under applications and forms, and it's the license application link.

It is up there. we have quarterly application windows that were instituted with reg change. the first one is coming up September 30th. We are doing an interim filing window, given we have gone from rolling to quarterly, and we're doing quarterly so we can prioritize applications based on the needs articulated in the statute and other underserved areas that we want to address capital access gaps for.

And so the interim filing window that will be coming up as November 1st, and after that it will be December 31st, et cetera. So at the end of every quarter.

MS. DUIGNAN: Jasmin?

MS. SETHI: Yeah, one of the issues we've talked about in the Committee a little bit is making information about all these different programs and government resources sort of more comprehensible, right?

We talked about this with the SEC's Capital Hub Navigator, which I've played around with, and you know, it attempts, I think, pretty -- you know, it's a good to kind of had a beginning to sort of having someone put in certain criteria and get kind of potential, you know, relevant regulations. So to kind of narrow down the world of relevant information.

So in an age of kind of where we have too much information, we have short attention spans, we're used to apps, we're used to gamification, you know, all these things that we may or may not or we're told may or may not be good for us, but they are here, for what it's worth, what are you guys doing to make this information easy to understand? Sort of pleasant to interact with?

You know, all those sorts of things?

MS. DEVRIES: I love your questions. You know, I'm a reformed marketer. So I will also share that those are also questions that I ask of my team all the time and I have just a very incredible boss and leader of our agency who is on a mission to make things customer first and technology forward.

As a note of context, and this might not be surprising, right? We do not control our budget. Congress gives us our appropriation and our budget and the SBA is the least funded agency with cabinet level representation, but we support over 33 million small businesses and over 2,000 intermediary's that provide financing to them.

And so there are opportunities for lift there, in terms of having the resources in funding to be in sync with the technology needs of today.

What we are doing, given the current constraints in funding that we have, assuming we don't have a shutdown at the end of the quarter, is focusing a great deal on revamping the information that's available on our website. It has been brushed up significantly.

And we also are working with outside marketing contractors to make our information more accessible. I think it's something where I'll just say, I don't think the federal government typically excels, in terms of attracting great marketing talent.

So it's a great opportunity for staff augmentation.

So those are my personal views. I am a political appointee. I will share that those are my personal views, but I think there's many opportunities for lift.

MS. DUIGNAN: Okay. Well, thank you, Bailey. We really appreciate you sharing this very valuable information with this Committee and the American people, and I want to thank everyone for the inciteful questions and presentations and this morning's very informative discussion.

For those of you watching us on SEC.gov, the Committee will return at 1:30 p.m. Eastern Time. So thank you so much for turning in and we very much look forward to having you back with us for the afternoon session where we have our second exciting agenda topic.

And with that we will break for lunch.

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

Afternoon Remarks

MS. DUIGNAN: Good afternoon, and welcome back to everyone who is rejoining virtually and on the SEC Webcast.

Before we launch into our afternoon topic, I'm pleased to welcome Commissioner Uyeda to provide some remarks to the Committee.

Commissioner Uyeda, I know you couldn't be with us this morning, but we appreciate you making time this afternoon to join us. Welcome.

COMMISSIONER UYEDA: Well, thank you so much, Erica. And yes, apologies for not being able to be with you and my fellow commissioners earlier this morning.

So good afternoon. As this is, I think, the second meeting for a large number of the members of the Committee, I hope that you're all settling into your roles.

And I thought I would share today some thoughts for your consideration as you formulate recommendations to the Commission during your tenure of service to us.

First off, one thought is that Commission roles should not be preordained to result in all or nothing outcomes. For example, the Commission may soon consider amendments to Regulation D including updates to the Accredited Investor definition.

A simple way to think about the Accredited Investor definition is a binary approach. A person can invest 100 percent of his or her assets, if he or she qualifies as an Accredited Investor even through either net worth or annual income tests, but if that person is a dollar short, then he or she cannot invest anything.

And this has been the approach for the last 40 years. Does this approach continue to make sense? At least not to me. The Accredited Investor definition seems to be simultaneously both overinclusive and underinclusive.

So one of the things that you could help us out at the Commission is to spend time to think about reconsidering Regulation D and the Accredited Investor definition and how it can operate to protect investors, facilitate capital formation, but also allow more opportunities to be shared with more investors.

For example, could an investor be permitted to invest a limited percentage of his or her portfolio or some other financial measure, given the requirements of regulations best interest and the fiduciary duty for investment advisors?

Could we be rethinking a different role for how investment professions -- how Regulation D deals with investment professionals? And these approaches may allow for main street investors to have exposure to gross stage companies as part of a diversified investment portfolio, but not keeping them out completely.

Second, the Commission's rules must address, in a meaningful way, any potential disparate impact on women and minority owned businesses and asset management firms, as well as historically underinvested communities.

While I raised this issue at the last Committee's meeting or the Committee's last meeting, I think it's worth emphasizing again because of the very large volume of rules that the Commission has adopted or may soon adopt and the cumulative effect of those could disproportionately impact these groups.

For example, last month the Commission adopted rules to impose additional requirements on Registered Investment Advisors to private funds. And one part of that rulemaking that I was very disappointed with is, I think that the final adoption release was dismissive to these concerns.

It said, well, minority and women owned firms can avoid the burdens of this by simply staying below the $100 million threshold to have to register with us at the SEC. And I thought telling these groups that the way you can avoid this is not grow your business just, to me, didn't make a whole lot of sense.

So please consider these two guideposts as you think about these issues. As you engage in discussions both at today's meeting and future meetings. As you carry out your duties on this Committee, I know you'll have the full support of the staff of the Office of the Advocate for Small Business Capital Formation.

I've worked with these staff members for many years now. Since the Congress created the Office in 2019, I know they've worked tirelessly to advance the interest of small businesses and their investors, and I think, over the last 16 months, the staff's efforts are especially deserving of recognition because they've carried out without a permanent director while also serving as the advocate for small business capital formation.

But notwithstanding this lack of permanent leadership, they have successfully hosted our Annual Small Business Forum, published the required annual report to Congress, and has helped organize six meetings of this Committee, and many more in the future.

So thank you very much and, again, thank you for your time and effort dedicated to public service and to be a part of our Advisory Committee on Small Business Capital Formation.

Panel Discussion Two

MS. DUIGNAN: Commissioner Uyeda, thank you for those really inspiring and informative remarks. So thank you.

So the overarching theme this afternoon is to look at various ways that small and early-stage companies access funding and where there might be gaps in that access.

Many small businesses do not have the kind of rapid, hockey-stick growth model that aligns with the expectations of most venture capital investors, yet, that does not mean that they may not be a good investment opportunity for the right kind of patient capital.

Before we head into that discussion, we are privileged to be joined by Karl Fooks, Outreach Manager of the State Small Business Credit Initiative at the US Treasury Department.

Karl has played a significant role in bringing to fruition a $10 billion federal program that was authorized by Congress in 2021. The State Small Business Credit Initiative is designed to support small businesses and promote entrepreneurship with a specific inclusion of underserved communities.

So it's our pleasure to have Karl here to provide an overview and update on that program.

Karl?

MR. FOOKS: Well, thank you very much for the kind introduction. Thank you to the Commissioners and the Committee members for this opportunity to speak to you and provide an overview of the SSBCI or the State

Small Business Credit Initiative.

I believe there's a brief deck that I sent over? Could that be shared?

MS. DUIGNAN: I think you can share it from your screen possibly?

MS. DAVIS: Hey, Karl, it's Julie Davis. We can share it for you if you prefer, if you --

MR. FOOKS: Yeah, that would be the easiest. Yeah.

MS. DAVIS: Okay. We will do it from here.

Karl, you just let me know when you want to advance slides.

MR. FOOKS: Okay. Please advance to the next one?

So I'm part of a three-member team on the SSBCI Program that focus on the equity programs. So myself, with Treasury, and then there's a contractor that we have taken on, Cromwell Schmisseur, Eric Cromwell, and Dan Schmisseur, who have specialized in state run venture capital programs for the past 15 years and they're assisting us in advising the states on their programs and the issues involved.

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So I'll cover a big overview of the program and then focus on some of the deployment numbers we're seeing as the program has started to roll out over the past year or so.

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So as mentioned in the opening, SSBCI was reauthorized as part of the American Rescue Plan in 2021 for $10 billion in funding. Now, this is a significant increase over the previous program, which came after the great recession in 2010, which the program was $1.5 billion.

This time there's specific allocations for tribal governments, an incentive allocation for the different jurisdictions to support underserved businesses, and a focus on very small businesses which we defined as businesses with less than 10 employees.

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So the SSBCI Capital Program provides an allocation to each state. So it's not a competitive grant. It's a specific allocation out of that $10 billion pool that each state has access to and they are required to submit a plan of how they intend to design and deploy small business financing programs.

And so there's generally five broad categories of financing programs that states use currently or its jurisdictions use. Capital Access Programs, these are effectively reserved against the pool of loans; Equity

Venture Capital Programs; Loan Participation Programs, Loan Guarantee Programs; and Collateral Support Programs. And all these have a different focus on different obstacles a small business may have in accessing its capital for its business.

And the jurisdictions look at their local economies, their local financial ecosystems and decide which mix of these programs makes the best sense for their goals and strategies.

The SSBCI Program provides a broad parameter around how these programs are designed. In particular, the private lenders and investors participating have to have a meaningful amount of their own capital at risk.

And the programs must be designed where the $1 of public investment by the program will crowd in and at least $1 of private financing and that, over time, the programs have to design an expectation to their programs that, over the life of the program, they'll crowd in 10 times the amount of federal contribution that has gone in to support these.

So it's very much geared to supporting and attracting private capital to support some of these underserved communities. And it's a focus on small businesses and what the federal definition of small businesses, generally 500 employees or smaller and $5 million average transactions size for most of these programs.

And in particular, the jurisdictions are allowed to contract with third parties, so there's not an expectation that they have to manage and administer these programs on their own.

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Specifically, on the Equity Venture Capital Programs, jurisdictions are able to provide two types of program design to their communities. A fund investment program where they can support the capital raising of venture capital funds in their ecosystem who then, in turn, invest in small businesses or they can implement a direct investment program where they are directly providing capital to small businesses alongside other private coinventors.

And we see a mix of these two types of programs across the country.

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So I'll provide you a data snapshot of earlier in the year of how these programs have started to deploy funds.

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So overall, about $3 billion now have been allocated by the jurisdictions to Venture Capital

Programs. So out of the roughly eight to nine billion that was provided for the SSBCI Capital Program, three billion of that has been specifically targeted towards Venture Capital Programs and this is a significant increase from 1.0, the earlier program I mentioned.

Similarly, we see the number of jurisdictions who are implementing Venture Capital Programs increased from the 1.0 experience to now 46 jurisdictions out of a total of 56, are operating Venture Capital Programs.

And they're operating multiple programs. So there's 84 Venture Capital Programs across the country, 48 being Direct-Investment Programs, and 36 being Venture Capital Programs, and many jurisdictions are operating both or several of each of the types.

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So in terms of how they have thought about this program choice between Principal Loan Programs or Venture Capital Program, you can see four jurisdictions have gone 100 percent Venture Capital Programs and their allocations.

And I should say the minimum allocation for a jurisdiction was around $56 million. The largest allocation was a little bit over $1 billion. So it was a range in between scale to the jurisdiction size, but you can see that over half have looked at allocations to

Equity Venture Capital at over 50 percent or near 50 percent of their allocated funds.

So pretty significant commitment to supporting this type of capital access for small businesses.

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And this is how it looks across the country. So the orange are the jurisdictions that have both a direct and a fund program, green are just fund, and the blue is just direct.

And I should mention Guam and American Samoa as the territories also have Venture Capital Programs. And the grey are states that have chosen not to have a Venture Capital Program and they're focused solely on credit programs.

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In terms of the scale of these programs, it's also very interesting. So 25 jurisdictions, so the nine plus the 16, are operating Venture Capital Programs larger than 50 million.

So that's a pretty significant increase in available capacity from the stateside. And again, they're required to match, at a minimum one-to-one with private capital and the expectation is, over time, they'll generate 10 times the amount of leverage on that specific allocation.

So it's going to be a meaningful impact on these local financing ecosystems. And if you look further down, 16 jurisdictions have programs larger than 25 million.

So again, historically, this is a significant support for state funded or state-run Venture Capital Programs across the country.

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In terms of dollar allocations to programs, this is the Direct Investment Program and you can see the largest is well over 120 million and drops down to, you know, around 10 million when you get to the smaller end of the spectrum, but for some of those jurisdictions, $10 million is still a very significant amount of money for their ecosystems.

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And this is a similar graph for the Fund Investment Programs. And again, some states have very significant commitments to support emerging fund managers in their communities.

The way the SSBCI Program parameters work, it's scales the participation by these state programs into early stage smaller, very, you know, emerging fund managers.

And so it's quite supportive, I think, of a lot of programs now that are looking to build more inclusiveness in the equity ecosystems across the country and many of the jurisdictions have specifically adopted strategies to support the deployment of funds to underserved communities and individuals.

So we're quite interested to see how this plays out over time. Many of these programs are just getting up and running in selecting their participants. And we'll be tracking the performance of these programs over time.

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So for reference to members in the audience, if you want to learn more about the SSBCI Program, these are some of the links you can follow.

The one at the bottom is the general website landing page for the SSBCI Program at Treasury, but then there are these specific policy guidelines for the Capital Program, compliance standards, and the frequently asked questions that might be of interest to you.

And with that I'll leave it to either questions or to proceed to the next agenda. Thank you very much.

MS. DUIGNAN: Thank you so much, Karl. We really appreciate that great overview and welcome questions from the Committee.

PARTICIPANT: I have just a quick first

question and that is, Karl, thank you for the information. it was very well put together. Can you state for us what are some of the reasons given by the states that didn't take their allocation?

And so why are there grey states? And what is the rationale there?

MR. FOOKS: There's a handful of states that had previously implemented Venture Capital Programs and for whatever reason the experiment did not go well, and they felt there would not be legislative support for further deployment, number one.

QUESTION: But they did the -- they did the Debt Programs, right? They just weren't doing the Venture Capital option?

MR. FOOKS: Correct. Correct. Every jurisdiction has adopted a program of some form and it's just some of the jurisdictions find that their equity ecosystems are too small. The business opportunity they want to support is better supported through a lending product then lending partners.

So again, our program allows for that program design decision and under 1.0, what we saw was there's an ability for the jurisdictions to change the mix of their small business financing programs over time and as they see the market dynamics play out.

When they submitted the application, it was one type of market environment, you know, as this deploys over the next five or six years, the market environments will change and they may change to choose their -- to change their deployment strategies.

So we will see what happens.

MS. DUIGNAN: Herbert, who's joining us virtually?

MR. DRAYTON: Thanks a lot, Karl. Great information. Just two quick questions. Are there any incentives for the states who are using the Venture Capital Program to engage minority or emerging fund managers? And then the second question is, can these funds be used to establish -- to work in concert within SBIC fund?

MR. FOOKS: To answer your second one first, yes, it can be supportive of SBIC Funds raised under that structure.

On the first point, I mentioned briefly in my opening that the reauthorized program had a specific allocation, which was held back from the jurisdictions, which is an incentive pool of money that, if they perform to an objective set for them for deployment to underserved communities and founders, that they would have access to this additional pool of money.

And so many jurisdictions who have implemented Fund Investment Programs recognize that the ecosystems need to be democratized and they are specifically trying to enable emerging fund managers from non-traditional backgrounds to apply for and get an allocation of funds because they think this will enable them to deploy effectively to some of these underserved communities and therefore reach their targets and then get their incentive allocation.

So there is some direction here for them to focus on these efforts.

MR. DRAYTON: Okay. Just a quick follow up. Are those objectives published somewhere?

MR. FOOKS: Yeah. If you look on our website, you will see the allocated amounts each date or jurisdiction received for this program, and one of those columns, they'll be what is called the SEDI or the Socially and Economically Disadvantaged Individual Allocation Target Objective, and that percentage of how much capital is being lent or invested into the companies if they can meet that objective.

They have 100 percent access to their incentive pool, and it scales back the further behind from that objective they achieve, and there may be an opportunity if they, you know, widely exceed that objective, there may be an additional bonus amount available to them.

MR. DRAYTON: Thank you, Karl.

QUESTION: I was wondering, in the SBIC presentation earlier today we learned that the funding provided by the SBIC is sort of expected to be a boat sitting on its own bottom, that they don't have to appropriate funds from Congress every year.

So I'm wondering, is this program similar in any way or is there any Evergreen aspect to the design of the program?

MR. FOOKS: The Evergreen aspect that we hope to establish is at the jurisdiction level. So again, the focus on these applications is these are not grants that the jurisdictions are making, but lending or investment programs where we expect the program design to enable capital to flow back to these programs.

So that once the Treasury oversight sunsets, the states will have built capacity and experience and have the capital that is returned to them to continue running these programs.

So the experience Treasury had was in implementing this the first time around in 2010, at a much smaller scale, the jurisdictions were able to build sustainable programs and many of them were operating at the time they applied for their reauthorized program.

But from Treasury's standpoint, you know, these are sort of one-time relief programs that are legislated by Congress and so we had to rebuild the team and reestablish the guidelines for this program and stand it up in pretty short order in 2021, 2022, to get the money out to the different jurisdictions.

So from Treasury's standpoint, not necessarily Evergreen, but from the jurisdiction standpoint we hope the program design and experience does allow for a similar experience of 1.0 that these will be significant programs that continue to operate over time.

MS. DUIGNAN: Questions?

I have a quick question just around just the concept of sort of state-by-state venture investing, particularly for smaller states that might not have a startup ecosystem large enough to sort of support its own investment ecosystem.

Are there any challenges there? Since I'm guessing that the allocation to each state must be invested and deployed within that state? Does that create issues for execution?

MR. FOOKS: So you're correct in that, you know, the smaller ecosystems have a challenge, but I would say the larger ecosystems have a similar challenge because, again, the focus of SSBCI is scaled to smaller earlier staged companies and the emerging fund managers and the states themselves have taken on a task of trying to build more inclusiveness into their ecosystems.

So even in states like California or Massachusetts, which are, you know, very robust, the ecosystems. They are targeting -- capital has not historically, you know, been abundant in.

So every state -- the beauty of this program is every jurisdiction, you know, has an opportunity to think through the opportunity set in its states for its economic development perspective and design programs around that.

For the smaller ecosystems, you know, who historically have not had a lot of private capital participation, we're seeing states get creative in identifying partners who can build capacity over time and I think one of the most interesting experiments that will come out of the SSBCI Program is this first-time allocation to tribal governments.

And there are many tribal governments who are also participating in Equity Venture Capital Programs, either individually as a jurisdiction or they have been able to aggregate into consortia, and these consortia are quite sizeable and are able to deploy funds over a broader geographic area because of the makeup of the constituent members of that consortium.

Also the SSBCI Program guidelines do allow for some of the investing activity to take place out of state. We put a cap on how much out of state activity can be tolerated at 10 percent, but we think that number is flexible enough to allow these smaller ecosystems to participate in regionwide funds, who can support the, you know, ecosystems of several states in a particular region.

So again, we're hopefully that both the private sector and the public administrators will find creative solutions and help build the ecosystems around the country. And we did see that type of effort under 1.0. It was just at a smaller scale and an earlier development phase of Venture Capital Investing, you know, outside of the main jurisdictions.

And so we think that experience does argue well for success in this program.

I should also mention that, you know, given that the focus of the agenda going forward is on alternative investing opportunities. There has been some interest from the jurisdictions and some from -- some managers for Treasury to consider, you know, non-traditional equity growth capital alternatives.

And so we are looking into this to see how it might fit into our statutory and guideline frameworks.

MS. DUIGNAN: Great. Do we have any additional questions?

All right. Thank you so much, Karl. We really appreciate learning more about the program. Karl Fooks, Outreach Manager for the State Small Business Credit Initiative at the US Treasury Department, which sounds like a really positive initiative. So thank you, Karl.

MR. FOOKS: Thank you.

MS. DUIGNAN: Wonderful. So as we move in to the second part of our day, I would love to jump into discussion around the second agenda topic.

We've heard some interesting sort of inspiring content on what the SBIC and SSBIC, or sorry, SSBCI are doing. So would love, as well, to open up the floor for discussion by the Committee on what we've heard today around this, as well as ideas for alternative funding structures and securities.

Jasmin?

MS. SETHI: Yeah. I'll just give a comment that kind of brings together some of the themes that we've heard today.

So I think, you know, and throughout our speakers today, you know, we've heard different issues of data come up. You know, we've heard diversity, underrepresented founders, we have different institutions, both government and private, using different definitions to allocate capital, and, you know, it's something we've talked about with the Committee before, you know, what are these definitions?

Is there a way to kind of maybe look at these different definitions? See if they're some consensus, and then also the data. So clearly private institutions are using data to allocate their capital accounting or diversity, as well as government entities are now, based on these incentive programs that we've heard.

And so, you know, what data are they using? What data is available and it occurs to me, you know, from the SEC perspective, you know, if other entities are using it, I assume the SEC can, if other government entities are using it.

So you know, are we leveraging all of that data to sort of make the most of it, in terms of the SEC reports and what could be done to make that data more informative going forward?

MS. DUIGNAN: Great. I think that's a wonderful point. Any thoughts on that? Any ideas that people might have?

No? Okay.

PARTICIPANT: I'll just make a comment. I mean, I think that we did get a lot of data today. and to the extent that that data can be included in the SEC report such that people who are investors, as well as people who are entrepreneurs, have access to things like the concept that there's 325 diverse fund managers out there or to the extent that they can find their way to the SBIC Programs, they can find their way to the SSBI, thank you for forging the way there.

MS. DUIGNAN: SSBCI.

PARTICIPANT: I think that that is something that we need to do is to get the data into -- consolidated because it seems to be pretty disparate across different places to me.

MS. DUIGNAN: Yeah, and I think that's one of the topics that we had discussed in June, was the idea of -- on the SEC informational website, being able to possibly link to some additional external sources of data and to all kind of keep track of other people who are doing the work, that we can then aggregate and hopefully make more available in the wider communities.

So I love that idea. One of the things too that I wanted to just note before we necessarily move on, and, in fact, first let me just put forth the question because the main agenda item for the afternoon that I'd love, I'm sure one of you guys probably has some really interesting thoughts on, is around other sort of potential types of securities for companies that aren't necessarily venture return projecting type of companies.

So has anyone sort of noodled on that a bit or come up with something very creative they'd love to share?

Bart, you look like you possibly have.

MR. DILLASHAW: So yeah, it's sort of an open-ended question. So this is an area that I sort of practice in and so like, yeah, there's a ton of stuff ranging from high-interest debt to sort of hybrid debt equity to sort of more revenue-based financing type of arrangements to pure equity.

So there's a lot out there and I think the way that I normally think of it is, there's a general spectrum of sort of risk/return and how the return is going to be deployed over time.

And at some level you need to have sort of a risk-rated return proportionate to the investment risk and then the return can be optimized either sort of front weighted. So you're sort of trying to get like a good IRR or sort of -- or called back weighted for like an ultimate multiple on investment.

Equity tends to be more back weighted because that's going to pay off when have sort of a final liquidation of a company because of a sale or IPO. Debt is going to be more sort of front weighted.

In terms of hybrid structures, probably the most popular one out there is something called revenue-based financing where the -- the concept is the investor makes an investment and will get paid back out of a portion of revenues.

So something like all right I will loan you x dollars and I want three x dollars in return and you'll pay me five percent, ten percent of your topline revenue. So the payback scales with the revenues of the company and then, you know, from the -- the investors basically taking a risk of what their IRR is going to be.

So it doesn't take 10 years to pay you back or it doesn't take two. So I just threw a lot of stuff out there, but that's sort of one alternative, if we want to talk about that.

MS. DUIGNAN: Yeah, I love that idea and you know as you were talking one thought that came to mind was around, you know, one of the main issues that I've had with equity crowdfunding for quite a while is that, in general, I don't think that 99.9 percent of the people who participate on those platforms have any idea how the valuation analysis actually works or what it means.

But what both -- and that goes for the founders raising money out in the platforms as well. So it's kind of like a meeting of two people who have no clue, and so everything becomes set wrong.

But what could be really interesting, and I think more realistic within that segment is kind of the idea of more of not necessarily affixed in some product, but in a bit of a hybrid, like, a preferred, right?

Which is that, hey, this is designed to not necessarily hamper the company, you know, with cash interest payments, but that it's designed to provide a return of 10, 12 percent a year.

So that everyone kind of in their mind knows like, here's what we're supposed to sort of pay these guys back and here's when they're supposed to get their money back.

So there might be a little bit more alignment because, you know, sort of a very nebulous concept of, oh, well, I own 100 shares in random startup that, you know, just decided it was worth $20 million.

There's very little understanding of, you know, what does the repayment look like, right? What is the exit supposed to be?

So I think that's kind of an interesting -- I kind of love the concept of working on some of these products specifically to address some of the lack of information, particularly around crowdfunding products, I think has made it very difficult for them to work.

Marcia?

MS. DAWOOD: So to that point, WeFund in January of 2023 put together a program that kind of molds together the equity crowdfunding alongside of revenue-based finance, where you can be a non-accredited investor, you can invest as little as $100, and you do -- it is an actual revenue-based financing model, not an equity crowdfunding model.

So that's one way. Then basically what he -- I just had him on my podcast and he was explaining the whole thing to me, that's how I know so much about it, but yeah, he was saying that a lot of Main Street businesses are getting funded that way because the people in the community are banding together to help the coffee shop, the dry cleaner type of thing because it's a very small amount of money that's needed, but it's also a way to get the investors paid back, you know, and usually it's like Bart said, like a two to three x and then they're done. It's not some egregious amount of money and it would be over, you know, a sympathetic amount of time. Maybe it would be, you know, quick, and maybe it wouldn't.

MS. DUIGNAN: George?

MR. COOK: Yeah, so a couple of thoughts. As someone who runs a funding portal, you know, the lack of transparency on funding portals around return expectations is actually partly because of the regulatory environment.

There's a lot of diligence that a lot of funding portals do, but we're not able to have a scoring mechanism that we're sharing with potential investors about how we're thinking about the risk of the investments that are being offered on our portals.

So actually, in a lot of ways funding portals are serving as that referee, but there's limitations on how we can talk about what we're refereeing.

And so there's some interesting opportunities there to relax those rules and allow us, as funding portals, to talk about what we're looking at and what we're not looking at to better help potential non-accredited investors understand the risks and potential returns.

And I'm really interested in this topic of revenue-based financing, which I absolutely love. The problem is, with revenue-based financing, you have to be able to accurately predict the revenue of a very small business.

Often with not great recordkeeping, often with kind of a very uncertain future, and if you end up overestimating the growth of that business, at the end of a revenue-based financing you will end up having a massive balloon payment for these businesses and a lot of these businesses will fail abruptly at the end of the financing term.

If you underpredict revenue, then the APR on one of the loans becomes astronomically high. So, you know, very interested in kind of how revenue-based financing can serve as that hybrid between debt and equity, but will also just warn the group that a lot of applications of revenue-based financing have been extremely predatory just because of a lack of understanding of being able to accurately forecast revenue for very young companies.

MS. DUIGNAN: Thank you, George. I was really interested though in what Bailey was saying though about the SS -- or SSBIC grant money, right? There's too many S's. And the fact that, you know, it was an accrued interest.

So I kind of wonder, and I mean, I just thought of this. I haven't thought it all out, but like is there a way that something like revenue-based financing could take that idea and be able to have this accrued interest possibility so that there could be a way that -- that it wouldn't be that detriment on the business, considering there are going to be ebbs and flows as the business is trying to grow?

PARTICIPANT: And also to address George's comment about it could be predatory because if you underestimate and the revenue goes way up then the investor is getting more of return.

Didn't Marcia talk about the fact that she was operating in an environment or what she was describing was capped?

So that the investors wouldn't get above a certain return even if the revenues did go through the roof?

MR. COOK: That's correct, except that the return period will accelerate. So if you think about it compared to a traditional debt product, the APR could become infinitely high.

We've seen revenue-based financing where the APR can be 4 or 500 percent.

MS. DUIGNAN: Well, I think that it's not a debt product. We wouldn't really want to think about it as PR, that would be my recommendation.

It's more of a hybrid of debt and equity to present companies, prevent companies who maybe aren't quite able to promise the, you know, 100x returns that firms are looking for, it should still give them an opportunity in the market.

So kind of categorize it a little bit that way in terms of thinking about returns because in venture the typical sort of annual return that deals are underwritten to is about 60 percent per year, so if we were thinking about APR, that would also seem very high.

So hopefully we could come to a happy medium.

But Diego?

MR. MARISCAL: Yeah, so I mean, I'm coming from my own perspective in my own work, but just in terms of thinking about sort of different types of funding structures.

So what we're looking at is setting up what's called a program related investment. So a fund essentially that takes on donations and then subsequently makes investments through a non-profit model.

So that's an interesting avenue to pursue, you know, whether or not you want to go down that path, I think that's a separate conversation.

But the other piece that we've been thinking about. Because we're able to utilize donations as opposed to traditional investment money, we are able to potentially use some of those funds to do sort of different types of lending.

So perhaps give preferential loan terms to certain communities at XXY, that just allows us to be much more lenient than a traditional fund would allow you to do.

So just throwing it out there as a piece of conversation.

MS. DUIGNAN: Marcia?

MS. DAWOOD: The other thing that people don't talk about very often or you don't hear about is using donor-advised fund money for private investment.

So there's a lot of donor-advised fund money. Billions and billions of dollars that are sitting out there not really doing much of anything, and a self-directed donor advised fund would allow people to -- it's kind of a triple win because you could take the money -- the donor does get a tax deduction.

They'll never see that money again, but it goes into a fund. It can then be invested into a private company or even a venture fund. And then the money that comes back goes back into the donor-advised fund, hopefully at that point more, and then can go to a 501(c)3 or a charity.

So then the charity is actually getting more money than they would have just off of a straight donation from the donor. And in the meantime, they're able to help these venture capital funds or these small businesses and I just -- the people haven't really started to talk about it too much yet, I think I'm hearing a little bit more about now, but it's definitely something to think about.

MR. MARISCAL: And I love that we -- just to follow up on that. I love that we've talked about it on the podcast specifically, like more in depth. So I think that also could be a good resource for people to just learn more about the different funding avenues.

MS. DUIGNAN: Yes.

PARTICIPANT: I think one that could be interesting that is very prevalent, particularly for small business is to have accounts receivable challenges -- so this is a simple process where you can sell the accounts receivables if the aging is significantly longer.

So if aging is 90 days, 120 days, instead of going out there to the sort of borrow money from a financial institution at a high APR, you can essentially factor and sell off the accounts receivable and then that would be at a fixed fee.

You don't have any risk of, you know, APRs ballooning, it's sort of set and it depends on the amounts that come in. So it's essentially selling the things that you were actually providing services for, rather than an assumed model that you can't control, especially from a macroeconomic perspective.

MS. DUIGNAN: I think that's a great idea.

Wonderful. Any other ideas around sort of products that maybe can be useful for these types of companies?

I haven't heard much from this side of the room.

MR. DRAYTON: I'd like to share three if I can?

MS. DUIGNAN: Oh, wonderful. Go ahead.

MR. DRAYTON: It's Herbert. Three -- I think I heard this mentioned. The conversation was dropping in and out. CDFIs, with regard to capacity building dollars. They are grants to organizations.

We are typically doing investments, but using those CDFI dollars, the training dollars that they have to provide assistance, maybe with a factional executive or to help with some of the marketing costs.

And someone mentioned earlier the use of donor-advised funds. There are a number of foundations out there that do have impact investing funds.

They're good organizations to partner with because they typically don't have the capacity to do due diligence on some of the investments of the small companies in the area. So they're great to partner with.

And then lastly, financial institutions and their CRA dollars. They're always looking for places to deploy capital. You may have to use a sponsor to get those dollars, but at the end of the day, we can move those dollars into some of the firms that we're investing in as well.

MS. DUIGNAN: Thank you, Herbert. Wonderful.

So anymore thoughts on sort of unique out of the box ideas for funding non-venture appropriate startups?

Okay. I think we -- go ahead.

PARTICIPANT: One question I would have for staff is, of the things that we talked about or you heard us talk about here today is alternative sources of funding. How many of those are on the information website that the SEC has?

MS. DAWOOD: Thank you. I don't know that any of them is specifically on the website. I think the challenge is the idea of -- well, obviously the website is structured that you've already gotten past the question of what is -- is what you're selling a security.

And so there is very, very high-level guidance on what is a security. Obviously, we wouldn't go into a very deep dive as to what is a security, so -- but once it's a security, we're agnostic, back to our sort of non-merit-based approach to regulation.

PARTICIPANT: So I guess the issue is if it's not a security, there's not information about some of these alternative sources of funding?

Would there be a way where if a company went and figured out that they weren't -- it wasn't a security or they weren't eligible for a security, would there be a way to just have high level information about other sources of funding for that company?

MS. DAWOOD: I didn't know if Julie was reaching for the mic.

MS. DAVIS: You go first.

MS. DAWOOD: I was going to say something very general like, I think that's interesting. It's something we can certainly consider what is in our purview to provide guidance on.

Maybe Julies got a more satisfying answer.

MS. DAVIS: No, it's definitely not more satisfying.

I was just going to say that, you know, I think -- we do have links on our website to the SBA and to some other government agencies that have a lot of programs from small businesses and this is part of, I think, the problem is that there are a lot of federal agencies that have small business programs, you know, the Minority Business Development Agency, there's just, I mean, I could start listing now and probably carry us through 3 o'clock.

So it -- our website cannot house them all, but I do think that they're not -- I think I've heard themes of conversation today where it would be helpful if there were some place where these types of resources could, you know, -- but even if they were all listed, you know, I'm sure Bart or other lawyers here can tell you that, you know, folks come in and they don't have a clue what -- they know I want money, they don't know if it's a security. They don't know if it's debt, they don't -- and that's something that takes a deep legal analysis.

So trying to find that information on a website, I think, is very hard and it's -- I have not seen government IT be able to crack that code yet.

MS. DUIGNAN: We could do like an SEC Hotline, if you --

MS. LEWIS: Are you offering to staff it?

PARTICIPANT: The other thing I'll add is that a lot of the stuff is on a local basis. So like where the capital sources are is going to be very locally driven.

So I would say in most communities, there probably is that website that will refer to the various local, state, national things that are probably applicable for that community. I think it's probably harder from a national level, but I will say that I think a lot of local communities probably do have a version of that.

MS. DUIGNAN: Jasmin?

MS. SETHI: Yeah. I wonder if this is something we can, you know, think about in the future. If this requires sort of congressional -- is this something that would be appropriate for sort of a congressional type action or direction of if -- if we wanted to have a centralized place where all information, all sort of government information, federal and ideally, even state, that's relevant to small businesses is in one place.

And you know, I don't think it has to be the most user friendly initially. I think if the information is there, private entities will, you know, if there's a demand for it, private entities will take it upon themselves to take that information and kind of find ways to market it and sell it and so forth.

But just to have that sort of government information in one place. So I wonder how would it make sense for the Committee to kind of proceed on that?

MS. DUIGNAN: Stacey?

MS. BOWERS: Building on that, I wonder a little bit if there's some kind of relationship with the Small Business Administration. I'm thinking about somebody that might have the that ability to house it who's not under some of the implications the SEC has about giving advice and things of that nature around securities.

So I wonder about that as well.

MS. DUIGNAN: Jasmin?

MS. SETHI: I think a lot of it has to do with just investor awareness as well. You know, we're talking about companies that don't need a ton of money, so there's not going to be institutional LPs, like banging down the doors trying to make investments.

So you know another thing we didn't talk about today, we talked about self-directed donor advised funds, but you know, people can also invest through a self-directed IRA.

And in this case, especially for people who are a little bit younger, they have the patience to wait, you know?

And I'm not just talking about for venture capital, I actually have a self-directed IRA and I did an investment in a debt instrument that helped a small business in the community and, you know, paid back over time and it was like a six-year kind of thing, and then at the end, they paid it back. They accomplished what they wanted to do.

So I mean, I think there's some interesting ways, but we also need to educate the investors as much as educating the entrepreneurs that these funding things are out there, because I don't know that there's a ton of people who would think, oh, well, let me go take my -- some IRA money and do something like that with it.

PARTICIPANT: Well, does it make sense to bring somebody in from the Small Business Administration to the next meeting who -- well, we can -- she's making a face like, well, I was going to say the --

MS. LEWIS: Yeah. Greg's with FINRA and Bailey is with the SBA, so she might be able to talk about it some at the next meeting.

You know, I do think that this is a problem that she -- she -- we -- our offices have talked about it and, you know, we each have our -- what is the word I'm looking for? Our mandate and limited staff and limited budgets, so you know I will just add in that our office did just recently put out a roadmap that, at the beginning -- it's on our website, and it does have some resources at the very beginning that hopefully will send folks, you know, if you happen to come to the SEC, which most small businesses don't.

They don't even know that we might be in there -- that they might need to think about being a security, but if they do happen to come to the SEC, the roadmap does show some places to go.

So it's something we're very aware of. Like, only six percent of small businesses end up issuing securities or raising money from investors.

So we're a small pieces of the small business -- I have a very, very important piece, my humble opinion, but you know, so I think we are aware of the issue, but I welcome -- I love all of these great brains thinking about ways to really reach people where they are.

MS. DEVRIES: I would just add on to that that similarly, for folks who have played with our navigator it sort of starts off with have you saw -- your other options for capital before taking on investors?

So we've tried, in our limited way, to address this question, but to Julies point and I think, as you have all heard me say over, and over again, if there are ideas to tackle that question more clearly and if we're missing something and there's a better way to put these funding options in context, you know.

We did this roadmap where you're going to start with your self-funding and if that doesn't work, you're looking at a grant or you're looking at a loan, and then when you get past all these curves in the roadmap, then maybe you're talking about investors.

So -- but if there are other ways that we can better share that kind of information, those kinds of resources with people, we are happy to hear suggestions. Thank you.

MS. DUIGNAN: Sounds like something to be gamified, the way you describe it.

George?

MR. COOK: Just maybe one helpful way to think about this. A lot of the financial products that we've talked about here at the table could potentially be a security, or they could potentially not be a security.

Debt can be a security depending on who's on the other side of the transaction. Factoring loans could be a security depending if they're, you know, trenched out and sold to a bunch of different investors or if it's just someone lending off their balance sheet.

So as we think about, kind of, within the purview of the SEC, all of these products could be relevant, but they have to fit within one of these exemptions and we have to think about who the investors are and if they kind of cross that line into becoming a security.

And to Marcia's point, there are a lot of different ways that we need to educate investors that these different asset classes exist and kind of when they are a security and how they can participate in these different types of investments.

So just a helpful, maybe, clarification.

MS. DUIGNAN: So I have sort of a fun idea that I've just come up with, being inspired by all the back and forth.

So when we think about how the SBIC Program operates, you know, which is mitigating the cost of the capital through, sort of the government guarantee, I do kind of wonder, I've always thought that when it comes to sort of crowdfunding initiatives, you know, these things really make sense on kind of like of like a hyperlocal basis, right?

So rather than like, oh, some person I don't know is trying to get me to convince me to invest in their startup, it's like, oh, wait, the local coffee shop or restaurant or whatever needs, you know, $20,000.

So there could be kind of an interesting mashup of the two where folks could kind of crowdfund from other people that are sort of in their local area, like, when we think about what the SSBIC, BCI is doing at the state level where basically the underwriting decision is kind of being made by the people that are in that community that actually use the product, but maybe there's kind of a layer over it of more like deploying kind of the backing of some of this sort of state funding programs.

Like, I think a hybrid there could be -- could be really neat. So you technically, you know, you do have to raise the money from people in your community or at least your state, or whatever, you know, have jurisdiction, but because the program's a state-run program, there's some more assurances around the safety of the investment.

Would love to kind of get thoughts?

MR. COOK: So I know the state of Michigan has a program like that. They will do -- I don't know if they do it for an investment crowd funding, but they do have a rewards crowdfunding program where if there's -- a community program to build a new playground, the state will come in and match the funds raised by the community.

I will say this is something that we're actively pursuing at Honeycomb, but we struggle with, again, some of the regulatory framework that we can't -- we have institutional investors who want to provide those matching funds, but we as a funding portal can't do that for them.

And so this capital is out there and it wants to come in and support small businesses in a matching way, but right now the regulatory framework makes it very hard to do that.

PARTICIPANT: Have you guys ever put together any type of recommendations on ways to change that?

MR. COOK: Yeah. I -- you know, we're still early days and kind of piecing it together, and frankly, no one's kind of figured it out.

So part of it is a language barrier a little bit, right? Of being able to kind of communicate that. Really it comes down to kind of the curation of investment opportunities to investors, which is a limitation of funding portals.

And then also funding portals are very, very limited on how they can touch funds of investors.

PARTICIPANT: Yeah.

MR. COOK: So even though the funds are out there, there's no on that can actually click the button and move the funds to where they need to move.

When I hear you talk, and I was thinking about it when I was listening to the discussion, it feels a little bit like a square peg, round hole, you know?

Or vice versa from a standpoint that we're trying to bend over backwards to find alternative ways of funding or getting funding, some form of investment into these companies when, you know, the bigger picture is the major players and whatnot, with the way the capital allocation works.

But maybe on some of these other ancillary issues, I mean, if you have -- you guys have thoughts on it.

I mean, you sound pretty expert in the area to share them with the group so that we can think about making recommendations as to ways to make the rules more workable for players like yourself who are looking to create a platform for alternative types of funding to find -- to find a home.

MR. COOK: Yeah. Absolutely. I think to Erica's point about the idea of kind of community underwriting, we're seeing some really powerful data, but just proprietary data internally, I'm happy to share with the group here, but our charge-off rates compared to the industry are a fraction of the industry average.

And I think that's really kind of speaking to the fact that there is local knowledge in small businesses and if you can leverage that local knowledge to bring other sources of capital to bear, you can do some powerful things to move money to chronically disinvested communities.

So happy to explore that further at future meetings.

MS. SETHI: And I just kind of want add to that, from what I -- I know a little bit about regulation crowdfunding, but the, I think the operational hurdles, in terms of the money, you know, that's something that may be sort of an easier and in some ways may be an easier issue to solve then the sort of curation aspect that you're describing.

So I think the issue with a curation aspect is that it gets very close to advice and my understanding of the motivation behind the crowdfunding regulations is, you know, we need a distinction between crowdfunding portals and broker-dealers.

You probably don't want to be regulated as a broker-dealer, because there's a lot more regulation involved, and that's the limitation.

So how do we give -- kind of figuring out what information is it that could be helpful to investors, but doesn't get into becoming a recommendation? Because once you get into that investment recommendation world, now you're in the broker-dealer world and, you know, that was the whole purpose of having this distinction.

MS. DUIGNAN: Stacey? One more comment.

MS. BOWERS: Sort of building on that and tying into what George has said, I do wonder, thinking about the intermediaries' obligations around education of investor and having to provide all the educational materials as part of Reg CF, without making a recommendation, is there the ability to provide additional educational materials?

And maybe you already do this and I apologize if you do, but sort of all of the things that investors should consider.

I mean, I know some of that's out there on a lot of the portal sites, but I wonder could there be a more in-depth exploration of, you know, here are all the things as a potential investor that you should be thinking about when you're assessing a crowdfund offering, whether they read it or not, I don't know, but that's all.

MS. DUIGNAN: Thank you for that.

PARTICIPANT: We should have the same disclosures for the lottery.

MS. DUIGNAN: Very, very funny. Wonderful. So given that we have about 25 minutes left, would folks like -- so there are two areas that I thought would be interesting to chat about before we wrap.

One, is thoughts from this morning. And then two is just another sort of quick overview around inspiration for next meeting's topics. So.

Would we like to start with any thoughts from the meeting with Fairview?

MR. COOK: Maybe just start with a question. And to Erica and to the group, but I'm kind of curious to understand where people feel the biggest challenge is?

Is the biggest challenge that there are not enough first-time, kind of new entrants into the venture space? Or do we think the bigger challenge is what we're starting to crack that nut, but there's not an opportunity for folks to graduate into larger funds over $100 million? Or is it both and?

Like, do we have a sense of like which is the bigger issue?

MS. DUIGNAN: So I think that those are kind of chicken and egg issues, right? I mean, I think that, you know, one of the things that we're pointing out is that if you can't start, you can't become big, and there are a lot of barriers to starting.

And so we kind of need to first make sure that people can start and then they can grow larger, but the, you know, the bigger sort of overarching issue that we are actually trying to fix is that there's a huge lack of diversity within the investment manager space, and so that results in a lack of diversity around how capital is deployed.

So generally, you know, you can't go into those giant existing funds and say, hey, change your whole checkwriter base, right? It has to sort of be done from the ground up.

But for that ground to happen, you know, is very costly, in terms of, you know, generally a new fund manager, you know, needs to have somewhere between five and ten-years of experience somewhere else, they have to save up a GP commit, they have to have a great track record, they need to be able to work without salary for probably the two years it might take them to raise their fund.

So that's just table stakes, and then, on top of it, folks tend to be biased. So we're just trying to remove the bias part, I think, is at least how I see the challenge and how the government might be able to help with incentives.

MR. COOK: Thank you.

MS. SETHI: But Erica, in your mind, is there something, because Commissioner Uyeda asked this in his remarks, is there something about the rulemaking that should be on more of a sliding scale for size, such that it -- I mean, I think we heard from Commissioner Crenshaw, Commissioner Peirce, and Commissioner Uyeda that they think some of the rulemaking is being burdensome on the diverse and smaller funds, and I think they're almost asking us to help them with that.

MS. DUIGNAN: Yeah, so I think he was referring specifically to the new private advisor rule, which I believe he says was going to kick in for people over $100 million and just that it would be costly and onerous.

So we do want to dig into that a little bit between now and next time. So absolutely. So that's something we'll -- I mean, there are so many different elements, I think, that touch the issue that we discussed this morning.

They're the ones that I had here with a star because it sounds so much fun, is what Commissioner Uyeda asked us around, oh, do we want to come up with some creative and interesting ways to redefine accredited investor.

So I was like, yes, I do. So I don't know if you guys feel as enthusiastic about, I think the leeway which he sort of described he would be willing to take ideas, but I thought that sounded pretty exciting for a next session topic, if you guys do?

MS. BOWERS: Well, and it would be very consistent feedback that they've heard that this body, in its many forms, has always advised them to make that change.

So if they're ready for that change, I think we should dig in and review that change. I mean, one of the big recommendations we made in the last Committee was that accredited definition, I liked his idea of the sliding scale.

Let's pick up and talk about that, but also to lean into somebody's experiential learning, education, you know, are they -- have they been an operator in a business? Have they worked at a bank? Et cetera, because knowledge of the industry and knowledge of how securities work should make it be that you don't have to have this big wealth cap, right?

You should have the knowledge, and that has never really been picked up before in the rulemaking. So I think we can definitely dive in to that.

MS. DUIGNAN: Well, I think it kind of is because even if you don't meet the financial criteria, if you work in the investment industry, you do get --

MS. BOWERS: If you work in it currently --

MS. DUIGNAN: Yeah. Yeah.

MS. BOWERS: But if you leave to do something else, all of a sudden, you're off -- your brain is supposed to be erased of all knowledge.

MS. DUIGNAN: You forgot everything.

MS. BOWERS: Yeah.
MS. DUIGNAN: Okay.
MS. BOWERS: I think that's a great idea.
MS. DUIGNAN: Who would ever get out of working in the financial industry?
(Laughter)
MS. DUIGNAN: Okay.
MR. DRAYTON: Erica, may I chime in?
MS. DUIGNAN: Yes, for a --
MR. DRAYTON: Yeah, just quickly. I think what the -- one of the things with the SSBCI funds that have committed to the states, I think one of the shortcomings is that they gave those dollars to the same folks that created a lot of the systemic barriers that are out there right now.
So if there is a way to require them to either engage with a minority, a woman, a disabled person to help them with deal sourcing, I think that would be great.
And the other thing is that maybe some of those resources could be committed to educating SEDI entrepreneurs who want to move into the venture space, and then maybe, once they graduate from those programs, provide some level of seed funding for their funds.
MS. DUIGNAN: I love that idea, Herbert.

That's wonderful. And just for more incite, I did not pick up on that during the presentation. So you are saying that -- because I thought these were going to like state-run venture capital funds that had specific inclusion targets. That's what I heard so --

MR. DRAYTON: Well --

MS. DUIGNAN: -- please elaborate.

MR. DRAYTON: Yeah, they've got targets. Like the state of South Carolina, we've got targets, but -- and I'm the beneficiary of SSBCI funds, but I wouldn't have known about them if I was not the Chair of a major foundation here in the region.

But there has been no -- they have not been intentional about trying to identify black or woman fund managers. They have been intentional with some of the resources they're committing to funds to let them know what the SEDI targets are, but they're not looking for, you know, black, brown, women fund managers.

Most of our resources have gone to white fund managers here in the state.

MS. DUIGNAN: Okay. That's great information and we should talk to Karl about that to make sure that they take that feedback. I love it.

All right. Wonderful. So anymore sort of thoughts, particularly on this morning's discussion?

Clarification? Ideas? What about the SBIC Program info? Was part of that news to folks or was everyone kind of already familiar?

MS. SETHI: I wasn't familiar. I thought it was very interesting and I love how they took the past information that they had and pretty much made it into something that was a little more doable for people.

You know, it's just that idea of a fund being able to pay back every six months, it's just crazy. So you know having that accrued interest is really interesting. So I'm really curious to see how it rolls out.

MS. DUIGNAN: I mean, I agree.

MR. DRAYTON: May I offer my -- may I offer my thoughts on the SBIC as well?

MS. DUIGNAN: Go ahead, Herbert.

MR. DRAYTON: One of the things that they -- and I haven't gone through and read through the latest rules, but one of the things that they did with the SBIC, those same requirements, you still have to have -- you have to have at least two fund managers with a track record to participate in the program.

So again, some of those barriers to entry, they just rolled into this program. Great program, but some of those barriers to entry are still there as well, and you have to be creative in finding partners to work with you, to partner with you to meet the requirements, because with that you have to have two fund -- two managers with a track record.

MS. DUIGNAN: Okay. I'm sorry. You said you have to have two managers with a track record?

MR. DRAYTON: Yeah. The program requires that you have at least two funds' managers with track records, I believe, of at least five years --

MS. DUIGNAN: Okay.

MR. DRAYTON: -- before you can qualify for the program.

MS. DUIGNAN: Okay. And I mean, do you think that sounds reasonable? Or unreasonable? Because that feels fairly reasonable to me.

MR. DRAYTON: Yeah, it sounds reasonable, but if you're going to get minority and women fund manager or emerging managers involved, I would tend to believe that if you've got at least one fund manager with a track record, they can coach and mentor and bring someone else into the space.

MS. DUIGNAN: Okay. Thank you. That's -- that is a good insight.

And unfortunately, Bailey is not here, but we'll pass it along to her.

Okay. So we have about 13 minutes left and would love to, number one, make sure we haven't missed anything that is really important for anyone to discuss, but also number two, talk a little bit about potential agenda items for our next session.

And you know, if I could start my idea that I think would be fun to include in the agenda, is that, you know, as many of us, as are so inclined, and hopefully that's 100 percent participation, that would like to sort of review the current Accredited Investor definition and come up with maybe a few sort of interesting twists or changes and we can all sort of go around and share.

I forget, one of the Commissioners said something in our meeting that if we had a magic wand and we could do whatever we wanted, you know, what would we do.

And so if you had a magic wand and could create a new Accredited Investor definition, what would it be? So you know, I think that when we're trying to solve problems creative ideas are welcome.

So would love for people to sort of think as much outside of the box as possible. I don't know if that seems like an interesting exercise for the Committee?

MS. SETHI: Yeah, I would second that and that's also very timely because they are working on proposed amendments for Regulation D and Accredited Investor, and the Committee has looked at it before.

So certainly, we should all look at previous recommendations. So that's something that could be impactful in the short term.

And then I think, just given discussions today, it sounds like other topics people may want to think about, whether for the next meeting or future meetings, is, you know, crowdfunding, sort of getting more information out there.

Kind of figuring out -- maybe getting -- we'll look into some speakers about this in terms of pooling together government information and making it just easier for small businesses to get that in one place.

And that may not be directly SEC purview, but we'll look into that as something for the future, because that sounds like that was of interest as well.

MS. DUIGNAN: Stacey, did you have -- George?

MR. COOK: Yeah, one thing I found really interesting this morning was having Eric talk about just the Department of -- or the Division of Corporate Finance. I think --

MS. DUIGNAN: It's actually Corporation Finance, as I learned after introducing him.

MR. COOK: There you go.

MS. DUIGNAN: For that --

MR. COOK: Which I think proves my point that I and I would have imagine some others around this table, even though we work with the SEC, might not have the greatest sense of how the different pieces of the SEC fit together and what all is under the SEC's purview.

So that might be something we can do asynchronously between now and the next meeting of just like a little bit -- kind of a high-level org chart and understanding what the different teams are, what the different teams focus on so that we can be thoughtful about what types of recommendations we're bringing forward.

MR. MARISCAL: I agree. That would be really helpful.

MS. LEWIS: Building on that, I wonder if it would be worth -- I'm not -- I'm not even entirely sure, as somebody who worked in Corp Fin, what the Small Business Policy Office, that's part of Corp Fin, I don't think it existed the decades ago that I was here, but I wonder if that might be a group. I don't know if it would make sense to maybe have them come in and tell us a little bit about what they do.

MS. DUIGNAN: Davyeon?

MR. ROSS: Just to confirm, and this is a question for the SEC staff. The SEC does have authority over QSBS, right? Tax – okay, cool. Got it. Okay.

I have, yeah. Okay.

MS. DUIGNAN: But it's an exciting topic. Why? What do you want to do?

MR. ROSS: It's out of scope currently.

MS. DUIGNAN: Oh, okay.

MS. LEWIS: Well, maybe talk to me later where the ACA is doing some work on that.

MR. ROSS: I think the largest thing is just working capital exemptions -- so that the exemptions -- there's a lot of things that probably won't make sense for small businesses at this point, so the way the current working capital exemptions is sort of structured, especially in a high-interest environment. So somebody to be cognizant of.

MR. COOK: And we can talk afterwards, but there's also a couple like bills pending on, you know, reducing the holding period and sort of liberalizing it out to sort of make it make a lot more sense and the works.

MS. DUIGNAN: The working capital exemption. Interesting. All right. If you say so. I love this.

I wish we could talk about this one in here, but you're right, I guess, it's out of scope. So all right.

Any other equally intriguing ideas? We just got a really juicy one there.

MS. LEWIS: If we're going to talk about Accredited Investor, kind of to Jasmin's point, they are, the Reg D and Accredited Investor are both on the agenda, so if we're going to look at the Accredited Investor to kind of be familiar with the whole review, they're going to make of Reg D, I think, would be a good idea.

MS. DUIGNAN: Do you guys have some videos for that?

MS. SETHI: Not on the substance of what might be in, but there was -- there have been prior proposals -- they're quite historic now. A couple of years, but (audio interference) past and kind of where the Committee has -- the Commission has gone to -- .

MR. DILLASHAW: And there is information on the website for the current exemptions and sort of how they work in practice right now?

MS. SETHI: Yes.

MR. DILLASHAW: All right. Yeah.

Closing Remarks

MS. DUIGNAN: Okay. Wonderful. Well, we would love to thank you all for an amazing discussion and to thank everyone who has joined us virtually or, I guess, they can watch a post-recording, or if you've joined us asynchronously, we hope that this was informative and interesting.

Our next meetings are scheduled for November 29th and February 27th.

I hereby move to adjourn the meeting.

All in favor?

All opposed?

Bart, what is it, Bart? Okay. The meeting is adjourned. Thank you, everyone, for your service.

(Whereupon, at 2:53 p.m., the meeting was adjourned.)

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PROOFREADER'S CERTIFICATE

In The Matter of: SMALL BUSINESS CAPITAL FORMATION ADVISORY COMMITTEE

File Number: OS-0001

Date: Tuesday, September 19, 2023

Location: Washington, D.C.

This is to certify that I, Kyleigh McGinnis, (the undersigned), do hereby swear and affirm that the attached proceedings before the U.S. Securities and Exchange Commission were held according to the record and that this is the original, complete, true and accurate transcript that has been compared to the reporting or recording accomplished at the hearing.

_______________________ 9/26/2023

Kyleigh McGinnis (Date)

REPORTER'S CERTIFICATE

I, Sonia Gonzalez, reporter, hereby certify that the foregoing transcript is a complete, true and accurate transcript of the testimony indicated, held on Tuesday, September 19, 2023, at 10:00 a.m. in the matter of: SMALL BUSINESS CAPITAL FORMATION ADVISORY COMMITTEE.

I further certify that this proceeding was recorded by me, and that the foregoing transcript has been prepared under my direction.

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