U.S. SECURITIES AND EXCHANGE COMMISSION

ADVISORY COMMITTEE ON SMALL AND EMERGING COMPANIES

Thursday, February 25, 2016

9:30 a.m.

Securities and Exchange Commission

100 F Street, NE

Washington, D.C.

PARTICIPANTS:

COMMISSIONERS:
Mary Jo White, Chair
Commissioner Kara Stein

MODERATORS:
Stephen Graham, Partner, Fenwick & West
Sara Hanks, Co-Founder & CEO, CrowdCheck

PANELISTS:
Robert Aguilar, CFO & COO, Cabrera Capital Markets
Xavier Gutierrez, President & CIO, Meruelo Investment Partners
Brian Hahn, CFO, GlycoMimetics, Inc.
Kyle Hauptman, Executive Director, Main Street Growth Project
Catherine Mott, Co-Founder & CEO, BlueTree Capital Group, BlueTree Allied Angels and BlueTree Investment Fund
Jonathan Nelson, Founder & CEO, Hackers/Founders
Patrick Reardon, Owner, The Reardon Firm
Lisa Shimkat, State Director, America's Small Business Development Center, Iowa State University
Annemarie Tierney, Vice President & Head of Strategy and New Markets, NASDAQ Private Market

PARTICIPANTS (CONT.):

Gregory Yadley, Corporate Practice Group Partner & Chair, Shumaker Loop & Kendrick LLP
Laura Yamanaka, President & Co-Founder, teamCFO, Inc.
Michael Pieciak, Deputy Commissioner, Vermont Securities Division

SEC STAFF:
Julie Davis, Senior Special Counsel, Division of Corporate Finance
Sebastian Gomez, Chief, Office of Small Business Policy, Division of Corporate Finance
Betsy Murphy, Associate Director, Division of Corporate Finance
John Roeser, Associate Director, Division of Trading and Markets
Joanne Rutkowski, Senior Special Counsel, Division of Trading and Markets

PRESENTERS:
Scott Bauguess, Deputy Director & Deputy Chief Economist, SEC Division of Economic and Risk Analysis
Brian Knight, Associate Director of Financial Policy, Center for Financial Markets, Milken Institute

PARTICIPANTS (CONT.):

Jeffrey Sohl, Professor & Director, Center for Venture Research, University of New Hampshire

C O N T E N T S

PROCEEDINGS

MR. GRAHAM: Let's get started.

Sebastian, do we have a quorum?

MR. GOMEZ: We do have a quorum.

MR. GRAHAM: All right. Hello, everyone. I'm Steve Graham. I am your co-chair. I am a partner at the law firm of Fenwick & West, and this is the beginning of my third term. And I think it's a great committee, and I'm looking forward to working with all of you. And I share the chair duties, if you will, with Sara Hanks.

So, Sara, do you want to give a 30-second -- or --

MS. HANKS: All right. I'm -- I am unable to switch on the technology. I am Sara Hanks. I'm CEO of CrowdCheck, which is a company that provides compliance, due diligence and disclosure services for the online capital formation, i.e. crowdfunding community. And I've been a long-time securities and corporate partner, and I am a proud former staffer of the SEC.

MR. GRAHAM: Okay. Thank you. So it's good to see the returning members, few though you are.

Catherine, nice to see you, and Michael. Michael doesn't bowl, but we love you anyway. And I guess we're waiting for Greg Yadley who is stuck in Florida. So hopefully he made it out.

MR. GOMEZ: He will make it. I think he's actually in the tarmac, Reagan right now, so he'll be here.

MR. GRAHAM: Okay. And the new members.

Annemarie, it's nice to have you sitting at the table. Now we no longer have to invite you to get your expertise. You're now required to be here. So it's --

(Interruption to audio.)

MR. GRAHAM: So to the rest of you, welcome. All of you are here because you represent a cross-section of those directly affected by or interested in or are otherwise qualified to provide advice to the Commission and its rules, regulations and policies as they relate to small business capital formation. I look forward to working with you to make a difference in this area, and thank you in advance for your time and efforts. Those of you who are new will soon realize the level of importance of the assistance given to this committee by the SEC staff. It is quite high and much appreciated, and thank you for all you've done and all that you will do.

We're honored to kick things off this morning with opening remarks from Chair White and Commissioner Stein. The other commissioner -- because we have two vacancies now -- the other commissioner, Commissioner Piwowar, also wanted to be here today, but he's traveling, so he sends his regrets.

Sara, do you want to introduce Chair White?

MS. HANKS: Yes, we are now going to hear from Chair Mary Jo White. Chair White was appointed in March 2013 by President Obama to serve as the 31st chair of the SEC and also the third consecutive woman to serve in that position. She arrived at the SEC with decades of experience as a federal prosecutor and securities lawyer. Prior to serving as the chair of the SEC, Chair White was the U.S. attorney for the southern district of New York, the only woman to hold that position in the 200-plus year history of the office and the chair of the litigation department at Debevoise & Plimpton in New York.

Thank you, Chair White.

CHAIR WHITE: Thank you very much, Sara. And good morning to everyone. I think I've shaken everyone's hand. If I haven't, I will later. And let me just extend a very warm welcome to all of our new committee members as well as the members who are returning.

This committee has been a continuing source of valuable expertise and advice to the Commission on a variety of important issues as reflected, I think, in the Commission's renewal of the committee's charter last year. You don't need me to tell you, obviously, that small businesses play a crucial role in our nation's economy, and this committee's help to ensure that the views of small business owners, investors and other stakeholders in this community are clearly heard loud and clear here at the Commission. So that I see as your role, and thank you for that role.

And I know from your impressive bios that I'm certain that this newly constituted membership will continue to the significant contributions we've had in the past. Each of you really does, as Steve alluded to this, raise unique insights and experiences in running, nurturing, advising and -- or investing in small and emerging companies. We know you have very busy schedules with multiple demands on your time, and we really sincerely appreciate your service on this committee.

I'd also like to add a special thanks to Co-Chairs Steve Graham and Sara Hanks for their willingness to lead the committee and also you'll permit me to extend an internal thank you to the staff of the division of corporation finance, in particular Betsy Murphy, Sebastian Gomez and Julie Davis for their heard work in supporting the committee's activities and helping to organize, obviously, the meeting today.

I know you have a full agenda, which you're anxious to get to, and so I'll just try to give a very quick update on our activities in a few areas of particular importance to you, including some that were actually the subject of recommendations from this committee last year.

Starting with the JOBS Act rulemakings, as you know, last year the Commission completed all of its major rulemakings under the JOBS Act, including Regulation A+ and crowdfunding, Sara. Since Regulation A+ became effective in June 2015, issuers have publicly filed over 60 offering statements with the Commission. Some of these issuers and others have, as you might imagine, taken advantage of the rule that allows for nonpublic staff review of draft offering statements before publicly filing.

The crowdfunding rules will become effective on May 16. And in anticipation, a number of funding portals have filed with us to register to serve as intermediaries in crowdfunding transactions. There's a lot of excitement about these new avenues for capital raising, and we are keeping a very close eye on how these markets develop.

In October of last year, at the same time, actually, we adopted regulation crowdfunding, the Commission proposed changes to Securities Act Rule 147 for intrastate offerings and Rule 504 of Regulation D.

The proposed changes are part of our efforts to assist smaller companies with capital formation while obviously maintaining investor protections. Your committee last year recommended that the Commission modernize. Securities Act Rule 147 to facilitate state-based crowdfunding initiatives. And that recommendation was fully considered in developing these proposed rules, which are outstanding.

As you know, I think most of you, the proposal taking account of the internet age, would modernize Rule 147 to facilitate intrastate offerings, including state-based crowdfunding offerings, which would be sold to residents of a particular state. The proposal would also update Rule 504 to permit offerings up to $5 million in a 12-month period and would make it consistent with other provisions of Regulation D, including a bad actor disqualification provision.

Comment period on these proposals closed in January, and the staff is reviewing the comments received and developing recommendations for final rules for the Commission's consideration.

On the topic of accredited investor, obviously that definition is a very important subject for us and for you and for many across the small business community and elsewhere. It's of particular interest to this committee and in making recommendations last year this committee urged that the primary -- always wise advice -- that the primary goal of the Commission's review of this definition should be to do no harm to the private offering ecosystem by constricting the number of investors who would qualify as accredited. You also recommended, including within the definition, those investors who meet a test of sophistication.

In late December a staff report was issued that analyzes really various approaches for modifying the definition and provide staff recommendations for potential updates and modifications. There's a comment file to receive the public's feedback on the report, and the issues and recommendations in it, and we encouraging all interested parties to give us feedback.

Simplified disclosure for smaller issuers. Last year this committee also put forward recommendations regarding disclosure by smaller issuers, including some changes in the disclosure rules for smaller companies as well as expanding the number of companies that qualify as smaller reporting companies under our existing rules that permit certain scale disclosures.

As you know, again, I think the staff in Division of Corporation Finance is advancing its Disclosure Effectiveness Initiative, which includes consideration of the disclosure requirements for smaller companies. We also now have, as of December, additional mandates under the FAST Act to update and simplify our disclosure requirements. So obviously our work in this area quite actively continues.

The committee also provided a recommendation regarding the regulation of finders and other intermediaries in small business capital formation transactions. Staff in the Division of Trading and Markets continues to review this issue.

The Section 4(a)(1 1/2) exemption, again, the committee last year supported formalizing by rule or statute the so-called Section 4(a)(1 1/2) exemption, to allow certain shareholders who may not be able to rely on Rule 144 to resell their shares received in a private transaction. This issue was addressed by Congress when it passed the RAISE Act in December as part of the FAST Act.

And I understand, Steve and Sara, that you'll be discussing the latest developments on this topic later today, and I really do look forward to hearing your thoughts in light of the changes made by Congress.

Just very briefly on market structure, we appreciate, the Commission, that while market structure may not fit all companies and that our market structure must promote capital formation for smaller companies while also obviously providing for robust investor protections. That is why we are conducting a pilot program that will be implemented this year to help assess the effective tick sizes on market quality for smaller companies. While I know that this committee's recommendation was to make some of those changes permanent rather than as part of a pilot, you should know how important your views were to the Commission's decision to undertake the tick-size pilot.

We also continue to study and remain receptive to innovative industry efforts designed to facilitate secondary market liquidity for smaller companies. So I wasn't quite as brief as I'd intended. So I'll stop there. I really do look forward to continued thoughtful and informed contributions from this committee on all of the topics I've mentioned as well as others. The focus of your agenda is, as usual, a good one. As I understand it, you'll first be discussing the current landscape for small and emerging companies seeking to raise capital and then reviewing what the current data shows about the extent of capital raising by small businesses through unregistered securities offerings.

As the avenues for capital raising are changing and evolving -- and indeed they are -- I think it's critical to be continuously looking at what's working, what barriers may be preventing the facilitation of capital formation and how investors are faring and being protected in these new markets. So again, I'll be keenly interested in today's presentations and discussions as I'm sure you will be.

So now I will stop by thanking you again for your service on this very important committee. Thank you.

MS. HANKS: Thank you, Chair White. And thank you in general for the SEC's attitude to this committee and helpfulness.

We're now going to hear from Commissioner Kara Stein. She's been a commissioner of the SEC since August 2013. Prior to serving as a commissioner, she served as a staff director for the securities subcommittee of the Senate Banking Committee where she worked on many financial services, including the legislation that became the Dodd-Frank Act and the JOBS Act.

Commissioner Stein.

COMMISSIONER STEIN: Thank you, Sara.

Good morning to everyone. I want to welcome both the continuing members and the new members of the Advisory Committee on small and emerging companies. I'm looking forward to hearing from you today. You bring a lot of energy to us. You're doing this pro bono, and we sort of count on you to tell us what's going on in real life. Sometimes we get a little egg-heady here. A lot of lawyers, a lot of accountants, and we don't necessarily understand what's happening on the ground. So your role is very, very important to us, and I hope you all speak freely and have robust discussions because that helps us as we try to formulate policy. In particular policy in how it might affect small and emerging businesses.

I want to thank our Office of Small Business Policy in the Division of Corporation Finance for putting this together. They spent a lot of time trying to work through an agenda that will use your time as well as possible while your with us.

So this committee has the important task of providing advice and recommendations to the Commission regarding privately-held small businesses and publicly traded companies with a market capitalization of less than $250 million. I think this year the committee will have an opportunity to examine a variety of novel issues impacting small and emerging companies.

As the chair mentioned, how will Reg A+ and Reg Crowdfunding work in practice? What are the best metrics we can develop to measure whether or not these new regulations are effective both with respect to their impact on small businesses as well as on investors? Which capital raising options work best for the firms that form a part of the small and emerging company landscape? It may be that the case that the fixes envisioned by some of the new mandates under the JOBS Act or other acts do not work in the manner they were intended. So this goes back to where reality sort of confronts people's best intentions.

So I'm curious as we move forward this year about your recommendations for helping us to understand and study what's happening in the actual market.

I think on a related point, are there asymmetries in access to capital raising options among small and emerging companies? Which companies are getting funding? Are capital raising opportunities, including the options available under Reg A+ and crowdfunding, are they known, and are they accessible on fair terms? And if not, why not? How can we best support the diversity of entrepreneurial talent that exists behind many of these small businesses. I look forward to discussions -- examine how women and minority-owned small business ventures are faring and how the Commission can help.

Finally, I look forward to the discussion today on the data, size and scope of the small business capital raising through traditional public offerings as compared to unregistered, private securities offerings. With the relative dollar amount of capital raising in the private markets in 2014 eclipsing that of the public market, we should examine what this means in particular for small and emerging companies.

Also, are small businesses receiving within the private markets the funding support they need to grow and eventually graduate to the public markets? So I look forward to your best thoughts today and the continuing discussion as the year progresses. And again, thank you for your public service.

MS. HANKS: Thank you, Commissioner Stein.

Now we'd like to introduce the SEC staff that will be assisting the committee and assisting the committee very well I might say. They're headed today by Betsy Murphy, associate director of the SEC's Division of Corporation Finance, and Betsy's going to introduce the rest of the staff.

MS. MURPHY: Good morning. Before going any further, I'm going to recite the standard disclaimer that any views expressed by an SEC staff member today are solely those of the speaker and do not necessarily reflect the views of the Commission or any other member of the Commission staff. That done, I would like to extend a very warm welcome to all of you and thank you for serving on the committee and for taking the time to be here today to share your experience, insights and expertise with the Commission and the public. We're very grateful for your service.

I'd also like to introduce the other staff members at the table with me. Next to me is Sebastian Gomez-Abero who is chief of the Office of Small Business Policy in the Division of Corporation Finance; Julie Davis, who is senior special counsel in the office. I think most of you know this, but in addition to coordinating with the Advisory Committee, the Office of Small Business Policy is the SEC's main point of contact with small companies. We also have John Roeser, an associate director in the Division of Trading and Markets and Scott Bauguess who is a deputy director and deputy chief economist in the Division of Economic and Risk Analysis.

I'll turn things back to you, Steve and Sara.

MS. HANKS: Thank you very much, Betsy, and all of you for your past and future help.

We're now going to turn to an absolutely impossible task. We thought it would be helpful to go around the table, have everybody introduce themselves and summarize their brilliant careers in 60 seconds or less. So if you could, each of you --

MR. GRAHAM: That will require brilliance.

MS. HANKS: If you would each to introduce yourselves and tell us a little bit about your experience and what led you here. Thank you.

MR. AGUILAR: Great. I'll start since I'm right next to Sara. My name is Robert Aguilar. I'm with Cabrera Capital Markets, an investment bank and broker-dealer, and Cabrera Capital Markets, an investment advisor with a real estate portfolio. I'm the chief operating officer and chief financial officer, and I'm happy to be on the committee.

MR. GUTIERREZ: Good morning. My name is Xavier Guitierrez. I'm the president and chief investment officer for Meruelo Investment Partners, which is a private investment firm in the arm of a family office based in California. We own and operate a number of publicly traded and privately held companies. And amongst our portfolio, we actually own and operate the largest Latino-owned bank based in California. So I will provide some insight in terms of the financing, Commissioner Stein, to the minority-owned and women-owned businesses in California that we face and we finance on a day-to-day basis. I also sit on the board of directors of the U.S. Hispanic Chamber of Commerce and I'm leading their efforts on access to capital for the 4 million-plus Latino-owned businesses in the United States seeking to access capital. Thank you very much for having me.

MR. HAHN: Sorry. My name is Brian Hahn. I'm CFO of Glycomimetics. Glycomimetics is an emerging growth biotech company that went public back in 2014. I spent 18 of my last 20 years at startup emerging growth companies. We've taken two of them public, but I've also been in manufacturing and technology. So I look forward to sharing some of those war stories and helping to kind of contribute back to that.

MR. HAUPTMAN: Hi, guys. I'm Kyle Hauptman. I'm currently executive director of a nonprofit here in D.C. called Main Street Growth Project. We're all about financial policy that is pro-growth and helps the little guy, loosely speaking, meaning small banks, small investors and the small businesses. I did start a startup in New York years ago and then I had a little bit of an odd career.

I'll just give you the short part of it which was after business school I wanted to get into finance, and eschewed some small opportunities and decided to go the safe route, and in 2004 joined a prestigious, solid company called Lehman brothers in '04. And then -- so anyway, I was there right to the end if you ever want to talk about that. I was shading repo trading if you know what that is, short-end trading, so I kind of had a ringside seat at that. But anyway, then I went to the think tank world and now happy in the nonprofit world.

MS. MOTT: Hi, I'm Catherine Mott. I'm the founder of BlueTree Allied Angels. It's one of 450 professionally managed angel groups in the United States. I'm also the founder of the BlueTree Venture Fund, which is also located in Pittsburgh. I'm chair emeritus of the Angel Capital Association. It's the nonprofit support organization for professionally managed angel groups and for individual angels. And I'm also the past chair of the Angel Resource Institute that is engaged in educating and professional development and research for angel investors in the United States.

MR. NELSON: Hi. My name is Jonathan Nelson. I'm the founder of Hackers & Founders. Hacker is Silicon Valley colloquial for clever problem solver, not someone who might be stealing your data.

CHAIR WHITE: I'm glad you explained that.

MR. NELSON: Every time I travel, I have to make that very clear. We started about 10 years ago with five people and me in a bar hanging out and talking about startups, and apparently hanging out in a bar and having nerds talk about startups is a thing, because there's now 115 event organizers in 45 countries around the world, and a quarter of a million people have attended our events. Out of that, we've built a consulting portfolio where startups pay us in stock for long-term services. Most of our companies come from overseas, land in the Silicon Valley, and then we help them globalize from there. And we've had conversations with literally thousands of tech entrepreneurs.

In a past life I was a nurse, and I also grew up in Central America, so the whole minority and women thing times to be kind of a thing for us. We have a blind selection process for access into our founders cooperative and consulting services. And as a result, our work was actually called out by the White House as being some of the best in minority support in Silicon Valley, which I think is really sad.

MR. REARDON: Hello. I'm Patrick Reardon. I'm from Fort Worth, Texas. I grew up in the Carolinas, so I've never lived in Washington or worked in Washington. Since I finished law school in '77 I've been in private practice for a variety of clients ranging from a client I have now that is literally a mom-and-pop real estate business run out of a house -- room in their home to working with Forbes 400 individuals. It's diversified and varied, and I've done a lot of things, and it may make me an expert on none of them, or it may just give me a diverse background. I don't know which.

I'm awed to be here, much less to think that the commissioners are listening to me for advice. Thank you for having me, and it is an honor to be here.

MS. SHIMKAT: I'm Lisa Shimkat, and I'm with America's SBDC Iowa. I'm the state director there. And it is a national organization and we actually just had our meeting here two weeks ago in D.C. and I told everybody then, and they started saying, oh, well, I need to sit down and talk about -- oh, I have another client, this is what they're running into. And I told them to wait until I had my first meeting.

But no, I am very excited to be here. I have experience in both private and public sector. I've worked with several different federal agencies, so have a little bit of that perspective as well and really looking forward to representing the small and emerging companies.

MS. TIERNEY: I'm Annemarie Tierney. I'm a vice president at NASDAQ. I oversee new market and strategy for NASDAQ private market. I started my career at the SEC, very proud alumni, with Betsy. In the -- I won't say when, in the early '90s. But I was in CorpFin, and then I went to Skadden Arps in London where I was doing IPOs and bringing companies to the U.S. capital market, and then I went to the New York Stock Exchange where I worked on corporate governance rules and listing standards. And then my career sounds kind of ADD, but it's kind of varied.

Then I was the general counsel of a dark pool broker-dealer, and then I became the general counsel of Second Market, which was, at that point in time, putting its toes in the private company space and that's really been my focus for six, seven years. And I'm very honored, as Patrick said, be a part of the committee, and I look forward to learning and contributing.

MS. YAMANAKA: Hi. My name is Laura Yamanaka. I am president and founder of a company called Team CFO. We provide outsourced CFO services for small and midsized businesses. I have a pretty traditional career. I'm an accountant by trade, went up through the normal public accounting ranks, did all the corporate reporting, compliance audits, all of that.

Got tired of that world and I thought there was a little bit more relevance in the small business world and foolishly just went out and started -- did corporate for a while, GE, all that stuff. And then foolishly decided to jump into small business world knowing absolutely nothing about what it was really like to start a small business, but I thought I did because in my corporate life that's what I used to do. I found out it was really hard to start a business when you didn't have a big old banking credit line and everybody standing behind you who had been doing it a for a couple hundred years. Quick learner or else you die. Spent the last 15 years in the small business world.

I also sit on the -- was chair of the National Women's Business Counsel. I also am past chair of NAWBO, National Association of Women Business Owners. It's given me a really good understanding of the broader problems across the United States that I see every day in our business life. I still try to keep a hands-on on what it's actually like to start a business through our clients, and actually in LA people were pretty excited that I was going to sit on this board.

They felt that the SEC sometimes has something for them that has no relevance in the small business life. So we started the education process. So I'm honored to be here, I'm excited to learn what's happening, and I'm proud to be able to give a lot of good input, hopefully, as far as the people who are slugging it out on the streets.

MR. PIECIAK: Good morning. I'm Mike Pieciak. I began my career working with small businesses at

Skadden Arps doing M&A transactions and such. But about two years ago I returned home to Vermont where I actually do work with small businesses on a regular basis working with our state-based crowdfunding initiatives and other ways that we assist small businesses. I'm the deputy commissioner of securities there, and I serve also as the chair of the North American Securities Administrators Association, corporation finance section, where we deal with issues affecting small businesses and larger businesses at the state level across the country. And I'm happy to be back on the committee.

MR. GRAHAM: Well, thank you all. Impressive. This is going to be great. As Chair White indicated, we're going to spend some time today beginning -- to lay the foundation for our term. Roughly the agenda is going to address the framework within which we are dealing, the nature of that universe, future steps, and of course your ideas.

So we all understand how critical it is for small businesses to be able to access capital. There are any number of approaches. I think we're familiar with all of them. The SEC's mission is to cover the securities side of the equation, and so therefore that is the focus of this committee.

Our committee's charter and bylaws provide that the committee's objective is to provide the Commission with advise on its rules, regulations, policies and policies with regard to its mission of protecting investors, maintaining fair, orderly and efficient markets and facilitating capital formation for that group that Commissioner Stein defined for us just a few minutes ago, namely small and emerging companies, the issuance of those securities, trading in those securities and public reporting and corporate governance.

For context as we do our work, we'd like to spend some time getting a better understanding of the size and scope of the nonregistered market. So this morning, we'll hear from the SEC's Division of Economic and Risk Analysis and to research organizations regarding the markets and the data currently being captured. This afternoon, we will turn to SEC initiatives and the continuing legislative activity in Congress.

For additional context, we thought it would be good to present a quick overview of the regulatory landscape. This will be familiar to most of you, but it might be helpful to just kind of refocus in the baseline.

So regardless whether security is equity, debt or a more exotic instrument, a basic fundamental of the federal securities law is that every offer and sale of securities needs to be either registered or exempt from registration pursuant to whether the exemption is the 1933 Act.

Turning to the public side, a number of small and emerging companies choose to go public and register their securities with the SEC. These become reporting companies subject to ongoing reporting obligations. Since Congress passed the JOBS Act, most new public companies start as emerging growth companies, and this status, of course, allows a company to follow scaled requirements for disclosure and audit of financial statements, not to have to provide auditor attestation under SOX 404(b) and choose not to become subject to certain changes in accounting standards.

This status will continue for the first five years after a company's IPO or if its total gross revenues are doing a more -- has issued more than a billion in nonconvertible debt in the past three years or becomes a large, accelerated filer, namely its public float is $700 million or more.

Prior iterations of this committee have also been interested in the definition of smaller reporting company. Currently a company qualifies as a smaller reporting company if its public float is less than $75 million. Qualifying as a smaller reporting company means a company has simplified disclosure and reporting requirements, including being exempt from certain disclosure requirements.

Last term this committee recommended that the Commission revise the definition to include companies with a public float of up to 250 million. Related to this would be a revision of the definition of accelerated filer such that the auditor attestation requirement under 404(b) would no longer apply to companies with a public float between 75 million and 250 million. And of course revision to the rules also would require revision of the rules to provide small reporting companies with the same disclosure combinations that are currently being made available to emerging growth companies.

We expect the term of the committee will -- we expect that this term the committee will continue to focus on these definitions and other ways to make the environment more conducive for small IPOs as well as the combinations for small companies that are already publicly traded.

Turning to the private side of the equation, Sara.

MS. HANKS: Yeah, so continuing Securities Law 101, especially for those who are listening at home, just as a reminder, Steve mentioned that the offerings must be registered or exempt. And if your offering doesn't fit within one of the exemptions that I'm going to talk about, either you're registered or you're breaking the law. This is kind of a binary thing. So you're going to register or you're going to fit within one of these exemptions. And some of these exemptions are very new. Some of them are driven by the JOBS Act. And because they're very new and, as Commissioner Stein mentioned, we're keeping an eye on how they're developing. A lot of these are going to be the subject of discussions by this committee over the forthcoming term.

So just a reminder, Securities Act Section 4(a)(2) and I think there's plenty of people who are old enough here that they're constantly saying 4(2) instead of 4(a)(2). So forgive me if I do that. That's the exemption that exempts transactions by an issuer not involving any public offering. The overwhelming majority of offerings under this provision, as far as we know -- and this is going to be a very important thing that we're talking about with respect to data and how much data we capture -- the vast majority of these offerings are done under Regulation D and more specifically Rule 506 which is a safe harbor under Section 4(a)(2).

Rule 506 comes in two flavors. 506(b) is what those of us who started doing -- practicing law in the '80s were working with. That's a traditional Regulation

D offering. And that allows companies to raise money privately, no limit on the amount of money a company can raise or the number of accredited investors. No general solicitation allowed under this exemption, so use of internet is somewhat limited.

Pursuant to the JOBS Act, this is one of the new ones, the SEC promulgated Rule 506(c) which allows companies to generally solicit potential investors over the internet so long as all of the purchasers are accredited investors and the issuer takes reasonable steps to verify their status as accredited investors. And we're looking forward to hearing data today about how and to the extent to which these exemptions are being used for private placement.

There's another private placement that I think we do have to mention even though must companies that we deal with are not going to be using it, Rule 144(a), essentially a private placement made under Section 4(a)(2) to underwriters immediately followed by resales to large institutional investors. Like I say, mostly used by larger companies.

Intrastate offerings, there is an exemption from registration for intrastate offerings. Section -- Securities Act Section 3(a)(11), the Commission adopted Rule 147 that we talked about earlier in 1974 as a safe harbor for companies seeking to meet the requirements of the 3(a)(11) exemption. One of the restrictions of that is the ability -- which we're going to keep coming back to I think a lot over the course of the term -- is securities law applies to offers as well as sales. And under old 147, you could only offer to -- and potential investors in your own state, which, again, limited the ability to use the internet.

Last September the committee -- this committee recommended to the Commission that it modernize Rule 147, and October 30, 2015, which Chair White had mentioned, the Commission proposed amendments that would modernize existing Rule 147 by establishing a completely new exemption from registration that would help to facilitate capital formation, including offerings relying on intrastate crowdfunding, which is a very new and developing thing over the course of the last year. And we'll get an update from Sebastian this afternoon on what commenters have been saying about the proposal.

Crowdfunding, something close to my heart. Federal crowdfunding is another significant development. The Commission recently adopted rules that will allow for the first time interstate securities-based crowdfunding transactions. New rules go into effect on May 16th, and we'll be hearing more this afternoon about what's happening as companies and intermediaries prepare to use these new rules.

Another JOBS Act-driven exemption is the many-IPO exemption of Regulation A. Regulation A+ also a very popular nickname for this thing, but anyway, it's an exemption that existed for many decades and in recent decades not very much used. But following rule amendments that went into effect in June 2015 due to the SEC implementation of Title IV of the JOBS Act, companies can now raise up to $50 million in a 12-month period if they go through a scaled SEC review process. And we'll hear more about Regulation A and the utilization of all of these exemptions both this morning and later this afternoon.

MR. GRAHAM: Thank you, Sara. I would just add that improved liquidity continues to be an imperative. I think that's one of the things that we all want to spend some time focusing on. Because for me, that's pretty much the long and short of it. And it is clear, as it has already been mentioned, that in terms of market structure to facilitate liquidity, one size certainly does not fit all. Smaller companies need a regime flexible enough to accommodate innovation and growth, yet strict enough to protect investors. And this is another topic that the committee has addressed in the past and certainly one that we will continue to be interested in.

There are just -- these are just some of the concepts that make up a landscape the committee will be delving into this year as we seek to help to insure that the views of small business owners, investors and other stakeholders in this community are clearly heard by the Commission.

Okay. We are pleased to have with us today Scott Bauguess. Did I get that close enough?

DR. BAUGUESS: Yes.

MR. GRAHAM: Okay. Deputy director and deputy chief economist of the SEC's Division of Economic and Risk Analysis. In these roles, Dr. Bauguess oversees the Division's risk assessment and custom analytics programs to enhance monitoring and investigation programs across the SEC, specifically in the areas of corporate issuers, broker-dealers and asset managers.

Dr. Bauguess joined the SEC in 2007 from Texas Tech where he was on the faculty in the College of Business. He continues to teach graduate courses and corporate financial policy at George Washington University. Dr. Bauguess received his PhD in finance from Arizona State University in 2004. He also holds a BS and MS in electrical engineering and prior to his doctoral studies spent six years working as an engineer in the high tech industry.

So, Scott, thank you very much for joining us.

DR. BAUGUESS: Thanks for that kind introduction. I was going to mention that my background as an engineer, it's somewhat of an accident that I ended up in finance and also ended up at the SEC. I never would have predicted this, but here I am eight years later, and it's been a wonderful ride being involved in initiatives like this.

Before we get started, just remind me the format is -- are we going to wait for Q&A at the end or can people interrupt?

MR. GOMEZ: Completely up to you, Scott.

DR. BAUGUESS: Okay. So if somebody wants to interrupt and ask a question, just push your microphone, and I'll pause and we can go from there.

So the disclaimer is already given. What I thought I'd do is just give a quick background of DERA just to let you know what our division does. For a long time we've been involved in the economic analysis, impact analysis for rules and regulations. We also support litigation at the Commission. We've done that for a long time, too. A recent innovation of our division is risk assessment. We're taking the same economic skillsets that we use in litigation and rulemaking and applying it to help Enforcement know, see, detect misconduct in markets and also to continue monitoring markets after rules have been implemented. And some of that you will see here in the data that we're going to present.

And to start, before I get into the background of some of the data that we're going to show today, I just want to quickly highlight that all of this work is not to my own. It's of three brilliant economists that collectively probably know more about the economics of the JOBS Act than anybody else in the world: Rachita Gullapalli, Vladamir Ivanov and Anzhela Knyazeva. And I put next to them the rules that they are particular experts in, and they not only helped develop the economic analysis in these rulemakings and releases, but they also continue to monitor the development of the markets and how they're evolving.

And to give a little bit of an outline of what I plan to do or hope to do -- and I'm sorry for those on the east side of the room if you're challenged and not being able to see the slides. But as to give some background of the landscape of the level of capital raising and where the capital raising is occurring, I think this is going to complement some of the other materials you're going to see following this.

And then it gives some general economic

perspective about how we thought of the rulemakings and the JOBS actually makings as they unraveled and share with you some or the predictions that we made as part of these rulemakings in terms of the likelihood of these markets working. In many cases, there's big questions about how well the rules will manifest and the actual practice of raising capital and then speak to some of the nuance of how we think about capital raising in terms of generating new capital versus just reallocating how capital is raised in markets.

And I'll run through very quickly each of the rulemakings listed there. Okay. So I'll also mention that we have now produce three white papers on capital raising, and each time we provide new information on how private and public capital markets worked. 2008 was when forms and filings -- or Form D became machine readable, and it was shortly thereafter that we really learned, maybe for the first time, how big private offering market was.

We realized it was a trillion dollar market in advance of then until the forms of machinery -- couldn't aggregate the data, and now we can. And for several years we've been putting out reports of the development. So you can see right here this is a chart that encapsulates that level of capital raising and dollar terms. So the 1,000 right there refers to a trillion dollars, which is a very big number. And we've broken out the first two sets of columns, the time series of registered offerings, debt and equity.

And you can see that the registered debt market is far larger than the public equity market, and I think that makes sense just because debt tends to be refinanced and rolled over. But what was somewhat surprising back when we did our first study and each year since is the level of the Reg D market and it was a nice introduction for Reg D and the rules underneath that was given just a few minutes ago. But you can see that Reg D, which is predominately equity-based securities, is tremendously large.

And the past couple years in particular it is larger when combined with other private offering exemptions than public capital raising. And this is an important point that private capital raising, private markets are very robust. There's a lot of activity going on there, and thinking about the JOBS Act, the JOBS Act rules is that interstitial set of capital raising that occurs between private offerings and public offerings and so how they will actually work in practice, what would keep -- what would get a Reg D issuer to use Reg A or not to be a reporting company is what we spent a lot of time thinking about.

If you look at the number of issuers during the most recently completed calendar years, you can see that there were 1,427. That should just be public issuers, reporting companies that raised capital either through SEOs or IPOs. Regulation D, there were over 1,560 -- 15,632 non-fund issuers. So this could be operating companies, finance companies, finance service companies, anybody that was not a fund. So there's a lot more entities raising capital in private markets than public markets.

And the fund, the pooled investment funds, hedge funds was another 16,000 issuers. Rule 144(a), which is predominately fixed income ABS type issuers, these are 4(a)(2) offers that are resold to qualified institutional buyers, and there were 1,418 of those. And then other private offerings and -- this is a little bit of a latent variable because we can't always observe private offerings if we don't have a source to collect that information. We had 268, at least that we've measured.

You probably have all seen this and known this, but it's nevertheless interesting to look at again, and that is if we break out the composition of public issuers in terms of their reporting status -- and here we show them as large, accelerated filers, greater than $700 million in market float, non-accelerated filers that are below $75 million in market float and accelerated filers in between smaller reporting companies, the SRCs that were previously described here, too, you can see that the composition of reporting companies is predominately non-accelerated filers and SRCs. That's a very large number, but they make up less than 1 percent of the market capitalization as far as we can measure whereas the large, accelerated filers make up 95 percent.

And what we've seen over the past decade, particularly since Sarbanes-Oxley, is that the number of public issuers has dropped from over 12,000 to less than 8,000. But the size of the public market is increasing, so there's fewer companies that are getting bigger. And from an economic perspective that makes sense because the fixed cost of being public has gone up. So it makes sense to be bigger. So that is something that continues to be the case.

We continue to see a number -- a decrease in the number of public companies, but they're getting bigger. And that's also the -- one of the reasons why the IPO taskforce looked at some of these issues that generated rules and provisions that were promulgated in the JOBS Act.

This was already mentioned, and I'll just highlight again in the rulemakings that we did, we thought carefully about small businesses and what was their role in capital raising, particularly in the crowdfunding release and trying to understand where entrepreneurs and business startups get their capital and typically it's with friends and families and nonconventional sources. And how will they be able to access more conventional sources? This was at the center of many of the discussions that we had in our economic analyses.

As I previewed in the outline slide and just to give you an idea of how economists think about capital raising -- and you would see this in the broad economic considerations and the introduction of any economic analysis that we have in our rules -- in terms of capital raising, we try to separate two unique concepts. And that is if we're going to change a rule or an exemption or an offering method, it could either cannibalize existing offering methods, or it could generate a new source of capital for issuers that previously could not access capital.

And it's not always easy to understand or measure the difference between the two, and both have merits. So if Reg A cannibalizes the Reg D market in terms of issuers simply switching over, that's a manifestation of a more efficient method of raising capital. But if Reg A were to attract issuers that weren't previously able to raise capital in private offering markets or using Reg D or big enough or have the resources to become a reporting company, then we would consider that a new source of capital.

I think that was probably the intent of the drafters of the JOBS Act was to create new capital, but both of these are things that we consider carefully and think are a benefit to the broader economy.

Okay. So what I'm going to do here is talk about each of the provisions in chronological order for which they were implemented or became effective. And I'll give you some views in terms of how we thought about these provisions and what we've observed. Some of this is our own observations that we've made from our analysis. Some of it's from the academic literature reports that have been made publicly since -- over the past few years.

And starting EGCs -- and I'm going to just do a quick disclaimer and ask my CorpFin colleagues to correct any mistakes that I make when talking about legal requirements of rules and to the extent that I get it wrong, but EGCs was -- I don't know if it was selfexecuting or occurred immediately with the enactment of the statute, but no rulemaking here. But after the introduction of Title I, what we saw is a large number of emerging growth companies, companies with less than a billion dollars in revenue, going public. It's about 12 percent of all reporting companies today, 928 EGCs and about 85 percent of all IPOs since have an emerging growth company status.

I don't actually have it on the slide here, but one of -- what's interesting is the literature today has somewhat -- academic literature today is somewhat mixed on the views of EGCs in terms of what that has done. The direct -- there's some evidence that direct costs have gone up to going public and also the indirect cost. So underpricing of IPOs with EGC status compared to beforehand has gone up.

And underpricing is the difference between the final day offering price and what the shares were sold to prior to going public. Historically it's been about 15 percent on average, and what it shows that EGCs, it's higher. That could reflect increasing -- information where because the provisions allow less disclosure or perhaps fewer years of audited financials, investors may price that as riskier and therefore have more underpricing. It could also reflect -- and there's evidence of this -- that a new type of company is going public that wasn't previously going public, which would be consistent with the intent of the EGC status.

So for sure what we see if there's a difference in pre- versus post-JOBS Act IPOs and those are the two general considerations that are being debated upon in the academic literature right now.

Let's see.

MS. MOTT: Scott, can I ask you a question? Again -- could you repeat that again? You said you noticed a pre-IPO price, so versus the actual price a difference? Is that what you're saying?

DR. BAUGUESS: Yeah, so underpricing is typically the difference between the closing price of the first day of trading and the share -- the price when the shares were sold to the initial set of investors.

MS. MOTT: So you think they were -- you're saying your data shows they were underpriced?

DR. BAUGUESS: So all data for the past 30 years show that offerings are underpriced, and the academic literature, not our research, but several papers have now shown that underpricing has increased, which means that the difference between the final day price and the initial offering price --

MS. MOTT: Okay.

DR. BAUGUESS: -- has gotten bigger. And the interpretation is that either is that they're risker, either because of the provisions of the EGC that are now available or because of the difference in the types of companies that are going public. So it's really hard to distinguish between the two. But for sure we know that there is a difference now.

MS. MOTT: Okay. I just wanted to make sure I understood it. Thank you very much.

DR. BAUGUESS: General solicitation for those here at the Commission that worked on this, it was a very interesting time because depending on whose view you were listening to, it was either going to destroy private capital markets and fraud and misconduct was going to promulgate at unprecedented rates to the view that this was the panacea for all investors or issuers that didn't have access to capital.

And in a nutshell, 506(c), and I'll show you some data, really hasn't been either of those things. It's been taken up at a very slow pace. We haven't seen increased incidents in fraud, at least discernably or measureable from our activities internal here. And we haven't seen that issuers are availing themselves to the ability to advertise and the removal of the ban on general solicitation.

If you look at our release that we -- the economic analysis of the adopting release, we made a number of predictions or claims. We noted that it was intended to facilitate capital formation, particularly for early-stage firms. And we thought that it would lower the search cost of finding accredited investors and also provide accredited investors with increased investment opportunities because they would be able to find investments more easily.

At least that the was the intent, and then if that were true, that would decrease the overall capital -- cost of capital raising and could potentially replace other offering methods. So that was the major prediction. We thought it might also reduce uncertainty as to whether 506 offering could be completed, and there's always the issue of release of information that may spoil the Reg D exemption and so there was a thought that this would actually help that issue.

And of course, the worry about the increased incident of fraud and economic terms broadly, the concern that that would erode investor participation in private offering markets. So that would be a negative spillover effect on the good issuers because of an increased number of bad issuers in that market. So those were the predictions.

As I said, we haven't seen an increase in the incidence of fraud. We have an internal JOBS Act taskforce and also a 506 working group that's headed by corporate finance and also works the office of market intelligence and enforcement. So there's special attention paid to tips complaints and referrals that come in. And over time, as these groups have met, we have not seen the widespread fraud that was at one time a concern of some constituents.

And at the same time, there hasn't been an uptick. 506(c) has not shown nearly the amount of activity that we thought.

Yeah.

MR. REARDON: I'd like to offer some anecdotal observations, and the first one is that large placement agents have -- such as Wall Street firms or even regional firms, have preexisting relationships with hundreds and hundreds of investors. And I've been involved in private placements where the offers and sales have been made to hundreds of investors in private placements before 506(c) was ever thought of.

My clients who are smaller clients since the enactment of 506(c) who are not using placement agents, but are rather going to investors and speaking to them, when I sit down with them and tell them that, well, you've got to tax returns or get a letter from an accountant. They immediately push back and say, oh, that's -- I'm never going to get anybody to invest if I start prying in their personal life like that, and it's just not going to work. And I'm not interested in that, so let's just do it the regular way.

Now it's anecdotal, it's not statistical, but it might be that the small fry for who I think this was really intended are just scared to go out there and say to these potential investors, well, I need to see your financial statements or get a letter from your accountant. And the reaction is, well, my money's green and I'll go somewhere else. And so, for whatever that's worth, you might consider that.

DR. BAUGUESS: I think that's a good observation and also my colleagues in the Division of Corporation Finance have much closer pulse to the views that have come in on issues like that. I don't know if they have any comments on that.

MR. GOMEZ: We've heard that, Patrick, that -- I think it's a concern that some have expressed. We've heard others' concerns as well. Anecdotally also, we've heard a lot of concerns with respect to the safe harbor verification at first, and then as time has progressed with respect to some participants a little bit more of a willingness to move to the principles-based approach of verification that doesn't necessarily require the issuer to go and ask for specific tax information. So it seems like it's an area that is still growing and developing. And it may be that people are slowly getting more comfortable with the principles-based approach and be more willing to move away from the safe harbor. But like yours, anecdotal evidence that we've heard from meetings with people.

MR. YADLEY: I agree with that comment. I think another element is still some concern particularly among lawyers and other professionals, but also among smaller issuers of not knowing who the people are. I mean it's a great idea to be able to get investors from anywhere, but then you think about these are going to be equity holders in your little business, and there's just a little bit of a fear factor there as well.

MR. NELSON: Can you double-click and expand on the principles-based approach? What is principled?

MR. GOMEZ: I'm going to move the chair. That way I don't have to squat.

So when the rules were proposed, the Commission initially proposed for taking reasonable steps to verify, there would be a principles-based approach in which the issuer would consider the information it has about the investor and make a determination as to whether the investor is accredited or not. During the comment process, the Commission has received a lot of comments from market participants and other observers who indicated that they would prefer to have a safe harbor for the taking the reasonable steps to verify. So in the adopting release, the Commission, in response to those comments, created two different ways of taking reasonable steps to verify.

On the one hand the concept of a principles-based approach, when the issuer looks at the information it has, it makes a determination it's one of the options. In addition to that, the Commission also added safe harbors. Now when you think of safe harbors, the Commission has to, in many ways, think about all of the potential different situations. So in many ways the safe harbor could have additional requirements that you may not have to go through if you're going through the principles-based approach.

MR. NELSON: Thank you.

MS. TIERNEY: I was just going to add that as second market, we had a business after 506(c) was adopted for about two years where we actually did verification as a broker-dealer for a number of companies that were utilizing it to raise capital. And I think what our experience showed was that, like Sebastian said at the beginning, the companies and the law firms that we were working with were very, very, very focused on the safe harbor and following the rules. And we worked with a number of issuers over two years.

I think the most interesting trends that we started seeing towards the end -- we don't do this business anymore, but towards the end where we really were seeing a significant number of letters coming from CPAs and law firms, which we thought was surprising. People really are not comfortable giving their personal financial information, even to registered broker-dealers, and we were surprised to see so many accountants step up and give certifications on behalf of their clients.

CHAIR WHITE: Scott, may I -- I think, but correct me if I'm wrong. I don't know how much data we have on this. But have we recently seen, in terms of the uptick issue, not an increase in the number of 506(c)s, but the amounts, the dollar amounts? I mean is that -- have you observed that or --

DR. BAUGUESS: I don't know offhand. I don't have the data here on whether the amounts have gone up. I do have a slide in terms of showing that it's been a steady state number of issuants over three years. But I'm sure that the crack staff sitting over in those seats is going to be able to answer that question in short order.

(Comment off-mic.)

DR. BAUGUESS: That's right. They're thinking about it. So let's see here. My clicker is now defunct. So maybe you can -- there we go. So on the point of the uptick of 506(c), one of the observations that I think is consistent with some of the reservations of doing it is that we see that the uptick is mostly with operating companies and not funds. And the many hedge funds, probably if they have to advertise the offering are signaling that maybe their offering isn't as good as those that don't have to advertise and there's some reticence to do so. But for operating companies or small businesses or companies, that is where we have seen the uptick the most. And I'll show you some figures on that in just a second.

But before we -- working again? Okay, great. Let's see here. But in terms of the use of 506(c), the intermediation costs -- so we see is that those who use 506(c), we thought -- at least we predicted in the rule that if you could advertise you wouldn't need to use an intermediary because you don't need to have somebody find you investors anymore.

What we actually see is that that those who do do 506(c) are more likely to have an intermediary, and those intermediation costs, basically what they report on Form D, are higher. So this was something that was inconsistent with what we predicted, but also consistent with of those who are using, they're probably new types of issuers.

And these are operating companies that previously may not have issued it, and now they're foraying into that market, and they're using a placement agent or somebody to help them and they're advertising in order to increase investor awareness of that offering. And also I should say the median offer is larger, but the amount raised is lower. So there's probably an increase in uncertainty and higher risk in some of those offerings.

This is a very busy chart, and it may be best to consume after the fact. But there are a couple of key pieces of information here. And the first is -- and there are four columns. And the first column is all 506 offerings, initial offerings, not amended offerings, so new initiated offerings that are captured on Form D. Since the enactment of 506(c) or the effectiveness of it on September 23, 2013 through the end of the last calendar year, there have been 48, almost 50,000 offerings and -- reported having sold $1.5 trillion. And most of that is in the 506(b). So 1.17 trillion is in 506(b), and only -- if you look at 506(c), only 23 and 26 billion were raised for funds and not funds. So you can see the overall level of capital is -- raised is much lower.

If you look at the difference between the average investors in an offer, 506(c) offerings for non-funds operating companies are only eight investors versus twelve for the classical 506(b), so they're a smaller number of investors. The offering size is also smaller. The median offer size is only a half million dollars versus a million. And it's interesting to note that the median size of a Reg D offer is a million dollars. Yet it's over a trillion dollar market, which means that the vast majority of offerings are tiny.

And it also helps provide context to other offering exemptions and state law registration preemption in particular that many of the smaller offerings that could avail themselves of other exemptions historically have used Reg D in the GAO report and others have acknowledged that's likely because of the preemption ability of the Reg D 506 offering.

MS. HANKS: Scott.

DR. BAUGUESS: Yeah.

MS. HANKS: I have a comment or observation on the number of investors issue because I think what we see in the 506(c) field, because you are able to use a special purpose vehicle, I think a number of the offerings do. So my guess -- and it's just a guess -- is that the low number of investors that you're seeing there very frequently includes one fund that has one fund that has 99 investors. Any way to get more information there and drill down on that, or we're just stuck with what's on Form D?

DR. BAUGUESS: Well, I hate to say stuck what's on Form D, because Form D even as written is brilliant. It gives us an insight into a market we don't have. There is also a pending proposal to amend Form D to collect other additional information that would help us understand better how that market's working. There are certain flaws with the way it currently works in -- not flaws, but inability to observe everything. And a lot of those caveats are highlighted in some of the work that we've produced. But we do like the Form D as it currently exists.

MS. YAMANAKA: I'd like to make a comment about that. When you made the statement that the average amount is a million dollars --

DR. BAUGUESS: Median.

MS. YAMANAKA: The median, that's really low, right? So when you go out there and you compare the cost of going through this process, you're probably -- this is not something they've done before. You have to access a whole different relationship pool from what you are currently providing versus going to bank and getting a loan for a million, which they probably have done multiple times.

From a cost-benefit perspective, unless you are planning to go through that route and you're making an investment in that area, it's probably not something you would really consider unless you really had a plan to expand your business and continually go out for additional funds that way. So the cost differential has got to be tremendous, loan for a million versus going through this route.

DR. BAUGUESS: Yeah, that's an excellent point, and it speaks to the broader issue. The whole idea of an IPO on-ramp was to create stages by which you could raise capital to ultimately go public, and that's a very astute observation.

This slide Chair White was asking about doesn't answer her question, but it does show that this is year-over-year changes and the starting date is September because that's when it was enacted. And you can see the vertical bars represent the number of monthly offerings, and the lines represent the cumulative number of offerings which is on the right scale. And it's almost scary how consistent this is over time. Going to the third year, there is zero deviation in the rate at which 506(c) is being used. I don't think anybody would have predicted that it would be such a steady state exemption in terms of issues availing themselves to it.

MR. HAUPTMAN: Scott, could I ask a question?

DR. BAUGUESS: Sure.

MR. HAUPTMAN: Sorry. I'm a little late to this I suppose. But could ask all of this on small investors and the companies that want their funding, how much was this benchmarked for best practices against other countries, like how does Singapore do this, how does Hong Kong do this to make sure we're doing it the best way? How much was looked at -- other countries were looked at in this whole process?

DR. BAUGUESS: That's a great question because whenever we enact a new rule or regulations, you have this issue of you don't have a counterfactual to what the world would look like with that rule in place. And often the only way we can do that is by looking at other markets to see what they've done, to look at disconnects and their changes of rules to see what happened to those markets. Unfortunately, even though our data is limited, it tends to be much better than what you can get in international markets. So we're often very limited and only have anecdotal evidence to speak on issues like that.

But as a point, maybe an exception to that is equity-based crowdfunding which has promulgated international markets probably in advance more so than here, and our rules were informed on those practices. And I think that even some of the -- that you might see later today is going to be drawn from that pool.

Okay. So I'm going to speed up a little bit here and just make -- give you some major takeaways from the Reg A rulemaking. And this is one that really does sit at the intersection of private and public capital raising and why would an issuer that would use the Reg D market, why would they avail themselves to Reg A and not do a public offering or why would somebody who's considered a public or registered offering avail themselves to Reg A or the modified Reg A.

And so a lot of the questions that we had -- and this is now -- we have six months' worth of data -- were centered on those issues. And I'm just going to point out a couple of things that we said in the economic analysis that we wanted to watch for and in terms of the potential use of Reg A. And there's tier one and tier two offerings. Tier two are exempt from state securities registration at or up to 50 million. Tier one is up to 20 million, and you have to register with the states securities authorities, but there are no ongoing disclosure requirements and different initial disclosure requirements, too, and I hope I didn't say any of that wrong, Sebastian.

But one of the things that we asked early on is why would you choose between the two, and it really is a tradeoff between the cost of qualification and ongoing disclosure requirements and the benefit of having access to a broad investor base and the preemption of those state securities, the registration process and the tradeoff between whether or not going general solicitation to accredited investors was better than going to retail investors and not having resell restrictions.

And all of that then hinges on liquidity, which somebody has mentioned earlier, of these securities of how you're going to exit this market. Will there be a secondary market that trades this, these securities? Are these Reg A issuers going to try to list on the big board or go national market exchange? If so, then they trigger 12(b) registration requirements which then has more onerous disclosure requirements. So the big outstanding question from an economic perspective is will there be an ability to get liquidity for these securities in such a way that it would provide a benefit over a private offering and also benefit over registering your securities and becoming -- with the SEC and becoming a reporting company, Exchange Act reporting company.

The data that we have today is somewhat limited, but what we see is that total capital sought is about 1.3 billion of qualified followings. That corresponds to 290 million. There's an even split between tier one and tier two offerings roughly speaking. And the median sought for tier one offerings is 13 million versus a tier two at 24 million and those that qualified -- or qualified filings, those are seven and a half and 23 million respectively.

If you look at who is availing themselves to Regulation A, they're mostly pre-revenue firms, so these are the typical startup idea generating firms, not the revenue generating firms. Now there's quite a bit of variation amongst the characteristics: issuer size, amount sought, industry location and profitability. Median assets is very low, so you can see that there's not a lot of dollar value of assets. And I think 72 percent of the filings had -- issuers had less than a million dollars in assets and 95 percent had less than a hundred million. And let's see here.

There we go. And some other observations, 90 percent of these are best effort offerings. There's no typical firm commitment offering like you'd see with an IPO. So you can see that these are higher risk firms in which the intermediation definitely has a different flavor to it than you would an IPO company. And most of them are equity offerings. The vast majority, about 80 percent, are equity offerings. Half of the filings are in business services, real estate and credit industries. I don't know that we had any preconceived notion what that would look like, but at least historically Regulation A had been a way to raise capital in the finance sector and banks in particular.

Yeah, question.

MS. MOTT: What was the other half? 50 percent were -- what other industries did you see represented?

DR. BAUGUESS: Maybe my colleagues in CorpFin know.

MR. GOMEZ: Catherine, we've seen pretty much every of the industry groups in the SEC that reviewed these filings have actually touched one Reg A offering. So other than that 50 percent that Scott mentions there, the rest of it has very dramatically --

MS. MOTT: So it's just varied.

MR. GOMEZ: Yeah.

MS. MOTT: So when I was looking at this and thinking about it, I mean -- and the reason I'm -- I guess I should say in full disclosure one of my portfolio companies is evaluating Reg A+ as an option. And when I think about the number of companies, it's in the healthcare, med tech. So I fully expected to see a lot of healthcare, med tech, maybe clean tech, some of the things that are more capital-intensive in that. So I'm a little surprised that business services is in there. So just wanted to try to understand. Thank you.

MS. HANKS: Actually, if I could add something on the nature of the filers, since I represent 10 percent of the companies who actually did the filing, many of the new companies are in what comes under the SEC filing categories of computer services. And one of the things we found in doing those filings, all of the options for industry type, you've got like left-handed widgets and right-handed widgets and big widgets and little widgets, and then a whole bunch of companies fall within one bucket, which the closest thing that we can find is computer services or in some cases entertainment.

So that I think is going to limit your ability to measure who's going through because we -- yeah, we're all computer services in one way or the other because we all use computers. That was the best thing we could think of.

DR. BAUGUESS: That's better than other.

MR. NELSON: And I just wanted to double-check. This is a total of 67 registrations and only three actually did the Reg A IPO. Is that correct? Is that the data that I saw in the previously slide?

MR. GOMEZ: So yes, so there were 68 Reg A filings in the previous slide. Keep in mind that the Reg A filing, once they file with the SEC, they go through a review process. And to the extent they're doing a tier one, also they go through a review process at the state level. And then once the review process is clear, then the company can still decide the timing as to when they want to qualify the offering.

So the previous slide noted that while there had been 68 companies that initiated the process, three of them have actually completed the process itself and their offerings qualify, which means that they can actually start selling.

MR. REARDON: If I can make a point, Laura, your question about why you wouldn't go to a bank and get this money is that under the industry comment there, business services, real estate and credit industries. Most of those companies are not going to be able to --

like business services, if they're like law firms they don't have any marketable assets though than a bunch of used desks that really have a tremendous discount.

Real estate traditionally is a combination of invested equity and borrowed money and credit industries is the same. Most of -- you first get the equity, you get your minimum amount of equity, then you go borrow the rest. And you have to have that kind of blend. So I would hazard a guess that most of those companies are looking as the next step to go to a bank, and they may even have a bank commitment letter. If X is raised, we'll lend you Y.

MS. YAMANAKA: Yeah, I think you're probably looking for -- this is just anecdotal based on the client base that I see in service and the people that I speak to. Usually at that point in time, it's friends and family. They have some sort of equity base first that they're building up. The next step then is a traditional banking relationship, which they're not starting out at a million. They're going out with a lot less amount. Then they're figuring out, oh, they can make some money at this in order to expand. How can we do it? A million dollars where I live is not that much, right, that we go.

And so I think perhaps a different industry -- because even we've got services firms. We actually particularly do attorneys, and a million dollars is nothing for attorneys. For all of you who extensive practices, you know a million doesn't go very far. So I think this point really illustrates it varies tremendously by industry.

And to the point, Sara, that you made, that's so true. Services, green tech, medical devices, medical services all get kind of lumped into that computer services which is probably distorting the information that -- Catherine, that you see or I see when I would classify the types of industries.

MR. GOMEZ: And one clarification, I misspoke when I gave you the data. Sixty-eight companies have filed with us. Seventeen of them have completed the process, and three of them actually have completed the sale or the transaction that they were doing, and they have reported that to us to indicate that they have completed the sale of the securities.

MR. NELSON: Is the -- any information on which three companies actually did that? I'd love to talk to them. Is that publicly available?

MR. GOMEZ: It's publicly available. I can talk to you afterwards as to how you get to that data.

MS. TIERNEY: Just if it may be interesting, we did a kind of deep dive into the Reg A+ space once the rules became effective to see whether there was an opportunity for NASDAQ private market to work with companies, especially in the tier two space. And we went into the analysis with some assumptions. Catherine, like, sort of that it would be med tech, healthcare, companies that had to constantly raise capital and probably would want to look at a different way of doing that.

So we talked to 14 different investment banking kind of companies, tier two, tier three investment banks, and their take on it was that their investors' primary focus is always liquidity. And so the inability to provide any liquidity in the -- even the tier two space because the resales are not preempt under state law kind of makes that a no-go for most of the banks to take their clients in that direction.

The other thing is they didn't see a real savings between a tier two 8A and an IPO using the onramp process. And IPO onramp provided more flexibility and kind of better accommodations. So they didn't see a real cost savings there. And then I think the other thing we were hearing was to the extent that a company did choose to a tier two with an 8A and they qualified to come to the market, they would do that. They would come to NASDAQ or they would go to the New York Stock Exchange, but it was really the absolute opposite of what we expected to hear which was very interesting to us.

DR. BAUGUESS: Those are great observations, and in particular the idea of raising equity to lever up to get capital in different ways is a little bit different than going public to get liquidity for your shareholders to cash out or list. And I don't think we captured that in our economic analysis, at least to the -- that wasn't among our predictions. So all these observations are really nice to have. Thanks.

MR. YADLEY: One of our clients availed itself of the new Reg A process. And their thinking was they weren't ready to do an IPO, but they wanted to get some visibility, wanted to start the discipline. Some of the things that I think we hoped would happen with this did use an intermediary. The process was very smooth with the SEC, but ultimately they were unable to raise the funds, so they withdrew. So positive experience except for where it mattered I guess, but the money was -- doesn't have anything to do with the rules per se, but we did a great job.

MS. HANKS: Only a lawyer would say that.

MR. YADLEY: But I think it does reflect sort of what Annemarie was saying is who are the investors and everybody wants everything, but what are they actually going to invest in, and particularly where they don't know somebody and they don't know the company. It sounds good, but you're still sort of gambling with an early-stage company.

DR. BAUGUESS: I'm going to finish very quickly there and just make a couple observations about crowdfunding, particularly since it's not yet effective. But just say from an economic perspective what we -- when we first started with respect to securities issuances, it was somewhat of a puzzle because it seemed to an economist that you had uninformed -- with respect to securities offering, an uninformed issuer trying to issue securities to an uninformed investor without classical intermediation. And how would you ever value that?

And so it was somewhat of a puzzle, and maybe our second question was wisdom of the what. And it took some internal education to understand with respect to investor protection. It really was a new way of thinking about how a crowdfund issuance or issuer might enter into the realm of securities issuances. But it was -- we spent a lot of time in the economic analysis thinking about how you would go from rewards-based to securities issuances.

The big outstanding question is still: How will an investor exit the security? When we talked to the Silicon Valley types a long time ago, we would often receive answers like, well, if you just do it, they'll figure it out. And you can imagine trying to write a rule on economic analysis of if you do it, it will work. It didn't meet the guidance that we have set forth in economic analysis.

But this is still something that we're very curious to see how it will unfold. We know there are ways a solution can develop and manifest, particularly with the creativity of Silicon Valley and already angel groups have demonstrated an ability to do this type of activity notwithstanding these rules and also state-level crowdfunding, so innovation is bubbling up, and there's a lot of learning going on and very curious to hear how this committee thinks or what they're observing and how this market will develop. And I'm going to conclude there and pass the torch.

MR. GRAHAM: Any additional questions?

MS. HANKS: Yeah, I just had one question, Scott, on the -- one of the sources, just to take you back to one of the very much earlier slides, I mean sort of the other lump. One thing that I always worry about this whole market is that we don't have a lot of visibility to the stuff that's happening that isn't doing

-- isn't relying on Regulation D or alternatively not filing Form Ds which in my prior life I did not use to do because it is not compulsory. And so I think there is -- I'm constantly looking at the data in tech crunch or any of those guys in PitchBook. Is there any way that you're looking out to see what you might be missing and crosschecking that? How much are you not capturing do you think?

DR. BAUGUESS: That's a great question. And we have done in similar rulemakings, particularly the bad actor release which is now a few years old, we compared Form D filings to prospectuses that are filed with FINRA and also ADV filings to see if there were evidence of issuers that were not filing Form D. And I'm going to have to jog my memory. It's been a couple years, but there was surprisingly good coverage with respect to not a lot missing, at least within that universe.

That doesn't mean -- I think I heard somebody once tell me that a private offering isn't private if you make it public through a Form D. And so to the extent that that exists, then you're just not going to see that activity, and I'll just throw it over to the CorpFin colleagues in terms of the outstanding proposal on Form D if they want to make any comments about how that issue may or may not be addressed if we ever picked that up.

MS. HANKS: I think that actually underlines my thought that if it's not intermediated, you're just not capturing it.

MR. GRAHAM: Well, there's -- I have a number of clients I'm sure that others are in the same position where like you said, Scott, if it's -- how is it going to be a private financing if you're filing a Reg D or a Form D? And I have many clients as a result that just done file because they don't need to. I mean the nature of the transaction is such that they're perfectly comfortable just relying on the statutory exemption. And there's a lot that is done in that area, as you know. I suppose you don't pick much of that up.

DR. BAUGUESS: We try to find other clever sources of information. A lot of this is self-reported through third parties for a variety of reasons, and it is a big, latent component of our analysis, but it is something that we try to get at. But unless there is a mandatory disclosure requirement or filing requirement, there will always be this unobserved component, and we just won't know what the level of compliance is with Form D.

MR. GUTIERREZ: I actually have a question on that. Sorry. Is there an intent on behalf of the SEC to then create a feedback loop, especially with the intermediaries to see what is happening out there actually on the streets, so beyond just looking at the sources, but actually bringing folks in and in particular those -- like I'm very curious about this episode in which someone kind of went through the entire process but then actually wasn't able to raise any money.

And so trying to understand what went right, what went wrong, what did they hear back from investors. Because as an investor, I certainly would love to know what is it that prohibited or precluded investors from actually pulling the trigger on something like this and whether or not that is a rules issue or is it just a comfort level with the process or possibly just with the types of companies that are coming back. So I'm curious as to what kind of formal feedback loop is being created in order to tweak what is out there.

DR. BAUGUESS: I know the Office of Small Business Policy gets information. Maybe they can speak on it. And I'll also just note that we do have a 506 working group that has offices and divisions across the Commission that we said we would do when the 2013 was -- and general solicitation was enacted. And we continue to monitor OC. Our Office of Compliance inspections examination often does sweeps. They got out and they talk to collect information that gets fed back. But I don't know if you have any comments on your operations, too.

MR. GOMEZ: Xavier, I think it's going to be interesting to see, especially in Reg A, because a company like the one that Greg was mentioning actually has made a filing with the SEC. That filing actually is qualified, so you know that the company went all the way through that process.

Now there's nothing that requires the company to tell us why didn't they actually sell. And I'm sure a lot of companies would rather not tell what was -- the problem was. I think we're going to get some data then with respect to companies that actually went through the process and still did not manage to sell. I think the harder thing is going to be actually the reason why that didn't happen.

Also, just one other thing that as an SEC staffer, it's almost like nails on the chalkboard when I hear that the Form D is not compulsory. The filing of the Form D is a requirement under the rules, and therefore it is required. I think, Sara, what you're referring to is the fact that it's not a condition to the exemption, so you do not lose the exemption if you fail to file.

But I think it's important to know for everyone here, which I'm sure you do, but also all of those -- you watching on the webcast, that the filing of the Form D actually is a requirement, and it does provide very helpful data to understand how the markets work.

MR. GRAHAM: It's a requirement if you're using Form D or Regulation D.

MR. GOMEZ: That's correct. And I think the point you were making --

MR. GRAHAM: But if you're using the statutory exemption --

MR. GOMEZ: -- Steve, is -- exactly. And I think a lot of the companies that get comfortable with the 4(a)(2) exemption and they feel like they don't have to go to the safe harbor in 506, well, at that point they're not relying on the safe harbor in 506(b). They're relying on 4(a)(2), and of course because they're outside of Reg D, then they don't have to file the Form D.

MR. YADLEY: That may -- and I doubt it's a primary reason why issuers would prefer to use 506(b) than (c), but certainly that puts it in the light -- you can't rely on the statute if you've gone out and tried to do a 506(c).

MS. HANKS: That's a really important point for the guys watching at home is all the stuff we were saying about the filing of the Form D not being -- it's not a condition, but it is a requirement. That's all going to be absolutely irrelevant if you are doing a generally solicited 506(c) because you've got to do that. Sebastian will be really mad if you don't.

MR. NELSON: Is there any way to get additional data on capital formation? As I've been thinking about being on this committee, I've been thinking, holy crap, this is a huge part of a GDP. Massive, massive amounts of jobs come from these tiny little businesses. But it feels like we're flying in the dark when it comes to how they have money. I don't know. Is there any other way to get that data?

I mean in Silicon Valley we tend to say what we measure we can improve. If we're not measuring it, we don't really know how well we're doing on capital formation from this. I've been banging my head against a wall asking people at Angel List, asking everyone that I know how would you measure capital formation. The best thing that I could find is could you get that data from like the IRS and tax filings?

I have no idea what the legality of that would be, but if you could actually look and say these startups or these small businesses had these capital purchases or this capital expense, and they had some sort of income, you could kind of infer from some of that. But I don't know if that's even possible or not.

DR. BAUGUESS: So you're saying that the Silicon Valley types would be for more mandatory disclosure on their --

MR. NELSON: I'm not -- I don't mind disclosing, but that's me. For me it's -- the question is not how do we disclose these stock purchases, but how do we figure out how small companies get their money.

DR. BAUGUESS: It's an excellent question, and we're always scouring for new sources, whether they're PACE service, fee services, vendor services, data aggregators, and we -- every new rulemaking that we promulgate, we think carefully about what the disclosure requirements are to the extent that it's within the SEC purview, not only thinking about what the disclosure requirements are, but how can we collect in a machine readable format in a very parsimonious way so that we can analyze it.

And so that's -- from an economist perspective, that's one of the first things that we look at, and that's one our contributions to the rulemaking process is to say here's how this data would be usable and here's what we would do it with it and help improve the efficiency of that process. But to answer your question on the IRS, information, data, it's a great idea, and I'm sure some of my colleagues in DERA probably know the answer to that question, but I don't.

MR. GRAHAM: Okay. Well, we're going to have to take a quick break. And so thank you, Scott, and let's break. Reconvene in 10 minutes.

(A brief recess was taken.)

MS. HANKS: Okay. Welcome back, everybody. Continuing the theme of data and what we do and don't have, which I think is going to be a constant theme for this committee for this term, we've got two experts here who can help us further unpack the information that is available or not available about the scope and size of the unregistered markets.

First we're going to hear from Jeffrey Sohl, professor and director for the Center for Venture Research at the University of New Hampshire. The Center for Venture Research has been conducting research on the angel market since 1980, and I must say it's very important research that I have looked at for a lot over the course of the last few years. Its mission is to provide an understanding of the angel market through quality research. Dr. Sohl specializes in early-stage finance of high growth ventures, trends in the angel investor market and entrepreneurship. He has a PhD and

MBA from the University of Maryland.

Following Jeff will be Brian Knight, associate director of financial policy at the Center for Financial Markets at the Milken Institute think tank. The Center for Financial Markets works to promote financial market understanding, expand access to capital and develop innovating financial solutions to global challenges. As manager for the financial technology and innovative capital access programs for Milken Institute, Mr. Knight is interested in the interplay between technological, regulatory and market innovation and how best to improve access to capital for business of all sizes.

Brian has experience working for a broker-dealer with a focus on the emerging online private placement market, and I am proud to say is a cofounder of CrowdCheck, a company which provides due diligence and disclosure services to companies and intermediaries engaged in online private offerings. He has a law degree from the University of Virginia.

Jeff and Brian, thank you very much for joining us today.

DR. SOHL: Than you, Sara. So what I want to do is just give you a little context, and let's see if this works. Where is my computer that I'm pointing to? Which one? Thank you. That is perfect, thank you.

So a little bit of history. This is back in 1874, so real history. This is probably the first angel investing we ever heard of. Alexander Graham Bell was looking for money and of course the banks back then thought the idea of a telephone was quite ridiculous as you can see from The Boston Post. And it was obviously too high tech and too advanced, and he didn't have any customers. Sounds quite familiar today.

Two angel investors, Gardiner Green Hubbard, who was a Boston attorney, and Thomas Sanders, who was a Salem leather merchant actually funded Alexander Graham Bell, changed the company, put it into Bell Telephone Company of Boston they called it. Alexander Graham Bell actually thought the first use of the telephone was to project concerts to people in rural areas, and Hubbard and Sanders said, no, no, no, no. We've got a little communications device here we're going to work on.

Fast forward that about a hundred years, and Anita Roddick opened up The Body Shop, one store, 1976 in the UK. And wonderful summer in the UK, very hot, sold tons of product, wanted to open up a whole bunch of stores. Well, the venture capitalist says, well, we don't do cosmetics, we don't do retail, we don't do that kind of stuff. So they found a gentleman named Ian McGlinn. Listen to this deal: 4,000 pounds in 1976.

That gave him 50 percent ownership in The Body Shop. That was his first ever angel investment. He was a garage owner. He owned a gas station. It was an extremely lucky deal. He came into the money through an inheritance. There's like -- you can't go into an airport or a mall or anywhere without a Body Shop today. So that's a little bit of context.

So where is this going? Just to see what investors look for. And again, I'm probably boring a bunch of people, but I like to look at the context because a lot of entrepreneurs think differently. Everybody thinks it's that surfboard. It's the technology, it's the idea. And in essence, the idea is one part, and in fact, it's not really that big a part. It's important, and I'm sure we've all in various walks of life had heard of, oh, I got this great idea.

Well, it's really that entrepreneur on top of that surfboard. It's the execution risk that you have to watch out for. It's how that is -- that idea is put to work, how it goes to market, how it's transformed from an idea to really in the market place. So that surfboard is great, and if it's a very good surfboard, but without that entrepreneur, it's not moving.

And I think the third piece of the puzzle that we always examine is that market niche, it's that huge wave of demand. There's a paying point out there, and there's a lot of people that really want that paying point solved. So that's that big wave. So if the surf's not up, as anybody who does surfing knows, you're not going anywhere on that board no matter how good the board or you are. So you really need that external influence of that market niche that's really flying along.

So with that in mind, the angel market and actually the private equity market -- and by private equity we all use various, different definitions. So I'm going to just look at it in this way. The crowdfunding, the angels and the venture capital. And I thank my colleagues at Crowdnetics, they gave me all the equity -- I just deal with equity crowdfunding, nothing else. They gave me all the equity crowdfunding data, over 6,000 deals since 2013. So that's good. That's of course accredited investors, because it's May 16, right, when the other rules go in.

The angel data is all ours, and the venture capital data is the National Venture Capitalist Association. So we look at the crowdfunding as really what I'm calling kind of the democratization of the private equity markets. We're trying to -- and the idea of the JOBS Act and the idea of all the regs is to allow the masses to now start writing checks in the startups.

And obviously I have my own opinions. It will be a great source of data I'm hoping, and it will be a fun ride for an academic analyzing that data. And I'll leave the rest of my thoughts quiet for now.

But so that really -- you've got the founders' money, and then you've got that crowdfunding kind of jumping in. The numbers were are getting -- now remember, this is 6,000 deals since '13, only accredited, so it hasn't really been fully democratized if you will. So here's some ideas.

Now be careful with that 20 percent success rate. Those are non-vetted deals. That's anybody can put the -- something up on any of these platforms, Angel List, anything like that. So these are non-vetted. They're not screened deals. There might be some minor screening, whatever the intermediary does, but nobody really screens it on the merit to my knowledge.

Now here's the ask -- and the raise, there is obviously a huge disconnect here. The average ask is 2 million give or take a couple hundred thousand. And the average raise is 210,00. So we are obviously not in sync here in those markets.

However, they are relying heavily on equity as one would hope. 72 percent of those deals are in the equity financing. 21 percent convertible debt. I just hope all those people understand what convertible debt is. And then about 7 percent is straight debt. My idea is -- my sense is that that straight debt probably has some kind of equity -- warrants something.

Now you -- I head when I was listening to the previous speakers, we were talking about sectors. And again, these are -- and, Sara, I agree with you. Some of these sectors get bumped in, so it's really hard to figure out what sectors we have. And again, this isn't the data that I collect, so I have to kind of -- it's not -- it's not an AX code level data.

But the best we could tell if you lump it, services is the dominant, about 40-some-odd percent in the services industry. Now that could be a whole bunch of stuff. And then technology is the 34 percent, and that seems like a lot of the -- oh, well, computer services, computer technology, yeah, we use all computers, so let's put it in technology. Consumer goods, which I thought would be a little bit bigger, is really small.

Healthcare, I remember the question -- I think that was you, Catherine, with the healthcare. That's about 5 percent, pretty tiny in the crowdfunding market, not so in the angel market. And commerce, I'm not sure what that is to be perfectly honest. But we literally just got this data. Luan Cox at Crowdnetics has basically said we'll give it to you ever year, we'll update it every six months for you. Have fun, and just give us credit. So we're kind of looking forward to having some -- there's some advantages to being an academic.

So these are our numbers on the angel market, and we go all the way back -- I just kind of cut it off at 2005. We kind of just go through one recession after another, so let's start in the last post-recession.

You can see what happens here. The market was humming along at about 25 billion. Right after the Great Recession or the whatever it was called, it got a little clobbered, and the -- down to about 19, 17 to $19 billion. These are still big markets, though. Keep in mind billions here. The deals really didn't change that much, and I'll show you on a chart.

But right now to give you the latest numbers, 2014, and we're collecting 2015 right now, we've got about 320 angels -- 320,000 angels actively investing in about 73,000 deals, about $24 billion market. My guess is in '15 you're going to see a slight uptick in that, probably not a lot of change. But here's the carnage, and you see what happened. It was kind of nice for us to see, not the carnage of course, but the deals actually held their own during the big drawdown. So valuations went way down. And it was easier to get in.

So the top line, which the big precipitous drop is the money going into the market. And the line -- and I'm color blind. So I think one of them, the darker one I believe is blue, is the one that is the deals. So that held pretty steady throughout the turmoil. And basically just valuations went down which in some ways is not a bad thing, and I'll talk a little bit about some valuations that are going on right now.

So if we look at the graph, and let's show where the gaps are here, that funding gap that's existing in the seed and startup market, that's not going anywhere, and you'll see some other numbers that indicate that it's not going anywhere. We clearly need some more money there. The angel groups that are there are doing a tremendous service to the U.S. economy, to job generation, to investing, but it's a lot of heavy lifting, and we just need more of that. We need some way, some clever public policy to facilitate the development of that market.

The crowdfunding, my best estimate is picking up that little piece of that funding gap. Some, which is nice, but I really don't see it filling in that whole gap because to be perfectly honest if you've got a deal, all things other equal and one of them has a hundred investors who never wrote a check before and they each have common stock versus a clean deal, you'd probably go with the clean deal. Again, that remains to be seen with the numbers.

Now what are the angels investing in? So now you're going to see the healthcare. The healthcare comes up. Remember those deals are going to take a bunch, maybe a couple more rounds, maybe some VC rounds. But there's definitely some dynamics in that market that works with the angel industry. And by the way, please feel free to ask questions at any time.

So the healthcare is always kind of a good one there, but the real soft spot is the software, and I shouldn't have used the term soft spot. But the software is -- you could take that deal and in many cases you could do two rounds as an angel, maybe syndicate the second round with some other groups that you work with and take that all the way to exit.

There's a lot of Dells and Microsofts and Apples waiting to buy some really good startups, avoid themselves doing R&D. It's a nice clean exit on a sale. IPO is a glamor exit, but, boy, a sale is nice, clean, there's no lockup period. It's usually a cash deal, everybody walks away pretty good. There hasn't been too much dilution.

So that's a very good investment strategy for the angel groups, and you're seeing about a quarter of the deals are in that space. Biotech has had its heyday. It's kind of up and down. A lot of that is the bioinformatics. The retail and media, be careful. That's really all the social media stuff, app development, all kinds of things like that. IT services, up and down. The industrial energy is the clean tech. It had its heyday in 2011. 2017 (sic) was a big jump. That was when there was a lot of government programs if you recall on the bailout money.

Now here's some hard numbers on deal sizes for angels. And this goes back from '08 to '14, so give you a little idea of valuations. Deal size is about 3 to 350,000 per deal. Now there's several investors in those deals, five to six investors. Each investor is putting about $75,000 in it.

Roughly around 10 to 15 percent equity is being -- this is maybe preferred stock, participating preferred, common, various forms of equity. That translates to a valuation somewhere between 2 and a half to 2.7 million. That includes U.S. That's not Silicon Valley, and I don't want to insult any of my Silicon Valley colleagues here, but they tend to -- the valuations may be getting a little excited out there shall we say. But I'll -- I have other data on that one.

Okay. Here's the yield rates. This is now vetted deals. So remember the crowdfunding was 20 percent on completely unvetted, through them up on the site. These are vetted. These are screened deals. By and large, they're screened deals. And so you're looking at yield rates. So you've got the denominator is the ones you look at, the numerator -- yeah, the numerator is the ones you actually invest in. Roughly around 10 to 15, 20 percent is the vetted deals.

Now when those numbers change, it's really tough. Is it a numerator or a denominator? More deals, more bad deals? You saw what happened, that number goes back to during the heydays of 2000 running about a quarter -- 25 percent, that's a little bit unsustainable. It's now running around 20 percent. A lot more people are understanding the angel market, especially entrepreneurs.

Let's turn to the venture capital market. Remember, angels 350,000 deal sizes, 73,000 companies roughly, $2 and a half million valuations. We got a 58, almost a $60 billion industry. These are not my numbers. These are the VC industry. 60 billion, almost 50 billion in 2014 industry. Average deal size is 11 to $13 million per deal and about 4,000 companies, not seed stage at all.

So here's the story. Because everybody remembers the story rather than those boring numbers. So there is a well -- this is a true story -- a well-known venture capitalist was visiting a friend of his. She had rented her garage out to two Stanford students who were, in fact, starting a search engine. She talked to them in the house and said, look, I've got to introduce you to these people renting my garage. And this VC who will remain unnamed, but is well-known, said let me see, two students, a search engine, no way. And his comment was: How can I get out of the house without getting anywhere near that garage?

Well, of course nobody took the flyer on Page and Brin except an angel investor, Andy Bechtolsheim, cofounder of Sun Microsystems, $100,000. If you look at the S1 forms when it went public, Andreas made quite a killing on that deal.

Seed deal, remember 4,300 VCs, total deals in 2015 of which 185 in the entire United States were seed and startup. It's not a seed and startup industry. And nor will it be for any time soon.

Now here's the scary part. Angels are typically the seed. Here's why we're seeing a little bit of a dilemma here. We're seeing a bit of an institutionalization of the angel market. Syndicating is nice. Starting to look like venture capital funds is not nice for the economic development and market perspective.

Now if that numbers an anomaly, I will be singing, you'll hear me all the way down here from New Hampshire if 2015 comes out back to about 50 percent seed and startup deals. 25 percent seed and startup deals means that we are really drying up that seed market. So here's the two problems here. You've got the crowdfunding taking the little piece, you've got the seed and startup even on a good day is tough, and then you've got the VCs pulling way to the right and so we're opening up that 1 to $3 million capital gap.

And then if you look on way off to that slide to the right -- and I have to mention this for sake of people talking about it, but if I hear one more unicorn, I'm going to get sick. These are $1 billion valuations. You realize there's only 230 of those worldwide. It bears watching, that's what I'll say.

Yes, Catherine.

MS. MOTT: Jeff, I'm really glad you're showing this because one of the things I've been thinking about is when I -- especially when I -- of course I follow your numbers, I give you our numbers.

DR. SOHL: That's right.

MS. MOTT: The average per deal with a VC market being about 13.4 million per deal, they're -- they've moved upstream. What I'm thinking about is is there a -- like an upside down bell-shaped curve so to speak? We have a lot of micro-investors, very few -- like VCs, we used to see a lot of VCs in 50 to 150 under management. But I don't know what the data is, and I'm sure NVCA has this -- has the data. But how many VCs are active in that 100 -- that 50 to a $150 million market? And how many are there that are a billion and over?

I mean where's -- so the gap -- my sense of it is there's a lot of angel investors out there, and you said it right. Even the angel groups have moved upstream and they're acting like micro VCs. We're syndicating, we're all starting -- I mean even the angel groups are starting to have microfunds that they're managing. But there's also this critical thing is the reason sometimes angels can't invest in new deals is because they have to invest in follow-on rounds to extend the runway to make sure those companies are successful because there are no 50 to $100 million funds in their backyard.

So I guess I'd like to see the data somehow sliced and diced so that we could understanding this funding gap is how many of the VCs all moved to these billion dollar funds and how many are available for extending the runway. And I'm just trying to get my head around what the data might look like.

DR. SOHL: Yeah. And we have that. I can give you a little thumbnail if I'm not held to actual percentages here. But you're absolutely right. And to follow up on your point, Catherine, that 1 to 3 million is that syndication, because, hey, somebody's got to do that round. You've got to do that second round. The VCs aren't going near that round now. And I always here, oh, Series A, the first VC fund. Series A is the first time you get outside equity. I don't care what you call it. But -- so somebody has to be in that 1 to 3.

We're seeing two players in that. As you said, the angel groups syndicating, getting a little bigger, micro-VCs. Then the venture capital market is getting a little bifurcated. There's these 20, 30, $40 million funds that could do -- they could move. Then you've got your 500, 600 million. They're not dinosaurs, they're the elephants, you can't move, you can't do a deal. You cannot do a 300,000, even a million dollar deal. It's not worth your effort to -- it's not economically feasible. So we're seeing a pretty big bifurcation in the market.

I haven't -- really I have not kind of played with the '15 numbers yet, but we're seeing that in the '14. So think of it as your upside-down bell-shape, the two ends are going to be the 20 to 50, maybe $100 million funds, somewhat nimble, can work in that 1 to $3 million range, and then you've got the big 200, 500, $700 billion funds. That's what we're seeing. And remember the good thing is deals come to -- I mean investors come to where there's good deals, so there's money to be made in that 1 to $3 million market. But again, my big fear is if that money gets reallocated from angel investing seed startup to angel investing post-seed, then we lose our acorns. And again, from a market perspective, that's my big concern.

And I think -- oh, I've got one more. Hold on. There it is. Abraham Lincoln. We're in D.C. I used to live here for 10 years. I used to love running around the Lincoln Memorial. So this is a quote. "I know of nothing so pleasant to the mind as the discovery of anything which is at once new and valuable." So classic angel investor statement. Thank you very much.

MS. HANKS: Thanks, Jeff. Can I take you back to one of the things that you said very early about the whole crowdfunding?

DR. SOHL: Mm-hmm.

MS. HANKS: It seems like you're treating the crowdfunding bit as a separate silo. And yet what I see in the market is anything that is online tends to be a kind of hybrid. Where you're going onto one of the funding platforms, you're getting some revenues from the funding platforms, but at the same time there's an offline portion of that. And frequently we see the ratio being 4 to 1 or 10 to 1 offline to online.

So two points, which is I think crowdfunding is not a separate animal here. It's sometimes -- in many cases, it is a separate extension. I'm also very dubious about some of the numbers I see from some of the platforms who say Company X listed on our platform and they raised $4 million. Where of course Company X did raise $4 million, but the bulk of it was offline. So how do you pass -- how do you control for that?

DR. SOHL: Yeah, and that's an excellent point. The thing -- the 4 to 1 and the 10 to 1, by your saying offline/online, online from online platforms and offline being angel group meetings and --

MS. HANKS: Traditional angels, yeah.

DR. SOHL: Sure. And those could possibly be two rounds, two separate rounds. Because the thing with the crowdfunding is, these are X shares for Y dollars, and as we all know with angels, you sit down at the table and that's all negotiable. And they're not going to --

you come up with I'll sell you X shares for Y dollars, and they're going to show you the door almost as fast as if you bring your lawyer. So I think the way I see that is the crowdfunding -- and I'm not seeing -- I do see them as separate. I'll be perfectly honest. Because I don't see the crowdfunding bringing the value adds that the angels do.

And I also see if you take a classic angel investor -- and again, we're all different obviously, but let's try to get to the mean a little bit -- is cash down entrepreneur, knowledge in this industry, active part of their portfolio, want to give something back, and this is full-contact investing. They enjoy this, they do it and they want to get a board seat and help everything.

Crowdfunding I see you cannot -- it's face-to-face in the angel market. Remember the angel market, over 90 percent of your deals are within a half a day's travel time of your principal residence. That statistic has not changed since 1978. And I mean that is amazing in today's world of Skypes and everything else. That has never changed.

So the crowdfunding is this distance-type thing where you lose the money where you lose the value add. So in some ways I do tend to look at it as a separate market.

MS. HANKS: And we do see these hybrid deals where we know there is a lead angel out there and sometimes they're even named, and it's usually piggybacking on their terms.

DR. SOHL: Right, but I don't consider Angel List as anything but a crowdfunding platform with an angel acting as a mini VC getting a carry. And maybe that's cruel, but I see the classic angel, they'll be a lead investor. Sure, there will be five to seven, maybe ten people doing the deal, writing, negotiating, sitting on the board seats. Angel List seems to me like an aggregator of somebody who wants to do and deal and lead it. So -- and I could very well be being way too harsh as an academic.

MR. YADLEY: So sort of a follow-up to that. As angels are aggregating -- and I think, Catherine, you've told us a lot in past committee meetings about how the organization is attracting more people to the angel networks and they're becoming more knowledgeable in bringing new funds. Do you think that there will be a cyclicality to this sort of like people get out of B school, and they want to work for Goldman Sachs, but as soon as they know everything, they want to be on their own or they want to go work at Fenwick & West and learn from Stephen, and then go off and start their own firm?

Do you think as these angels -- will they morph into these sort of mini-funds as you've described them and then go out because I believe what you said, that people want good deals, and they're jealous of the good deals, and they really don't like sharing information about the best deals. So do you think there may be sort of a pendulum swing back to smaller, maybe one or twosies in the angel world?

DR. SOHL: Yeah, and certainly there's -- my crystal ball gets a little cloudy at times even though we're not supposed to say that as a snotty academic. But sure they're going to go where the deals are and where the returns are. So if there is, as is going now, this retreat from seed because the 1 to $3 million deals are pretty sweet. You've got a little bit of runway, you've got a little bit of customers, slight less risk, a little closer to exit, not much, but a little closer.

So there's -- and there's not a lot of players in there, not a lot of competition certainly in most parts of the country except that area in the left coast. And so you've got -- so the money would normally move into that. It's a return, risk-return tradeoff. Now as that then retreats, then does the seed and startup market become that much more attractive, less players, better deals, much lower valuations. Maybe just no runway or a little bit less, but you can get to that second round runway. So yes, it will take the long-term or maybe long-term in this industry is three years maybe.

What I fear is that in the meantime we may really lose the seed market, and then -- and that could be too draconian. I just would like to see a little public policy, keep an eye on that seed, because that's hard work. It's really heavy lifting. And any way we can help angels in that market. We've done a lot of work in Europe, and matching funds at seed and startup deals, boy that helps a lot.

I mean these are not -- these are federal level funds over in Europe where they can grab a certain amount of money on a 4 to 1 basis where the angel puts in let's say 400,000 and 100,000 comes from some other fund. They ride along in the terms. If it's a success, that fund grows and it's -- but it's a government fund, but not a government-run fund.

That kind of tweaking would at least give me a little more solace that that angel market will always -- that seed and startup market will remain a viable entity and then possibly scoot up and down. No, even out the troughs, because I don't want to be in a trough too long.

MS. MOTT: Jeff, in addition to that, I spent some time in Europe last week with the angel groups, or I mean last year. The -- it brings new angels to the marketplace because they're -- it derisks some things for them and allows them to learn how to be sophisticated investors. So those matching funds have done well in Canada as well.

DR. SOHL: Yeah, we did the -- we helped designed what we call the Archimedes Fund, the lever. That was the Netherlands, that was Belgium. They're doing very good, those funds. That's where they got the term from, but of course they spell it differently. And then the Canadian work we've been doing, Canada is very -- I think they're pretty astute on watching that seed market.

MR. NELSON: So I was just -- a couple of other little data points. We've actually worked with the White House and Mayor Bloomberg's office on immigration for entrepreneurs coming here from overseas. And when they created the Entrepreneur in Residence program at USCIS, they were actually able to open up an 01 visa which means exceptional talent visa for entrepreneurs that came who had gotten funding on one of these crowdfunding platforms.

Because if I'm not mistaken, the statistics are there's about 140,000 startup profiles on Angel List and less than 1 percent of those get funded every year. And so it's harder for you to actually raise money on Angel List than it is for you to get into Harvard. And I absolutely agree almost all of it -- it's an introduction platform, and it helps angels become kind of mini VCs and be able to help syndicate the deal for some of the hard work.

Another data point that you had asked, Samir Kaji, who is director of private equity at First Republic Bank, recently published an article on CB insights. He was tracking about 100 funds in the sub-$30 million range that had popped up in the last year and a half. But those funds are essential because before I introduced one of our companies from our community to them, I'm asked to have that company have between 5 and $10,000 a month in recurring revenue and growing 7 percent month over month before I introduce them to a seed fund. So in my mind, a seed fund is now growth equity.

DR. SOHL: But again, that's that 1 to #3 million pot in that what I call post-seed. So it may just be semantics.

MR. NELSON: That would be -- these are funds that ostensibly write 250 and 500K checks.

DR. SOHL: Yeah, but I mean seed -- I always think of seed as not really having a lot of runway yet, but again, that's just -- it's semantics. The VCs will

swear they're seed investors because they're looking from one end down and vice versa.
MR. GRAHAM: Okay. Thank you, Jeffrey.
DR. SOHL: Okay.
MR. GRAHAM: There might be other questions, but we wanted to get to Brian. And so after or during your presentation, Brian, we'll continue to ask questions, but why don't you go ahead and get started.
MR. KNIGHT: Thank you, Stephen. And thank you, everyone, for having me here.
So thank you, everyone, for having me here. I'm Brian Knight. I'm from the Milken Institute Center for Financial Markets. Part of the work we do looks at access to capital for small businesses and the implications of financial technology in that and other spaces.
So last year, in conjunction with the National Center for the Middle Market, we did a survey of 636 owners and c-suite executives of private companies -- there were a couple of public companies that slipped in -- -with total annual revenues ranging from under a half million to a billion dollars. The survey was administered last January to early February. The goal was to provide a snapshot of how these companies are accessing external capital, how they anticipate accessing

external capital and what is -- what factors they consider when looking at external capital.

Our key findings, one, that debt was the preferred method of outside financing, that firms when they were evaluating methods of outside financing they valuated the price that they were going to have to pay to get the financing obviously, but also the ease of access, the speed of the funding and the certainty that they were going to get the funds in good order.

Firms were uncertain about whether bank or non-bank financing was superior, but a lot of these firms had strong preexisting relationships with their banks, and that was cited as one of the major reasons why they used bank funding.

At the time -- and this may be a little bit stale, because of course this was pre a lot of the JOBS Act provisions actually becoming effective -- there was a low level of understanding and a low level of interest in these potential models. And we'll see some of the actual data on that here shortly.

First we asked these companies what methods of capital have they used in the past three years. As you can see, the -- it was a tie between a loan from a bank and they didn't raise outside capital. They just operated off retained funds or they didn't exist three years before. After the bank, the next options were operating on retained funds or a loan from a non-bank lender, then a debt investment from family and friends, then money from a family office, then an equity investment from family and friends. So you had to get pretty far down on their list before you reached an equity investment.

The types of firms that -- or the types of debt that these firms had, bank debt was a predominate model across revenue bands. Private debt increased the larger a firm got, roughly speaking, and the smallest firms were more likely to have no debt at all.

We asked them in the -- and then this next year, so it's a year that just passed, how do you anticipate funding your expansion plans. Cash on hand was the largest answer, then going to existing -- their existing credit facilities. 20 percent had no plans for expansion, and 19 percent said that they would take on additional debt, and then everything else fell into an 8 percent bucket.

DR. BAUGUESS: Can I ask a question?

MR. KNIGHT: Sure.

DR. BAUGUESS: How did you select these 600-plus firms, and what was their general characteristics? What was the identification method.

MR. KNIGHT: So first we used a survey firm to identify -- there is -- we went for a -- we banded it by tiers, and I don't have -- I believe it's in the -- I should mention we have -- the report's available online, and my colleague, Jackson, in the back here has copies if you want them.

We tried to match revenue band and industry with their representation in the broader economy. And then we used a nationwide survey, so --

DR. BAUGUESS: I asked because I'm wondering how much is growth firms versus somebody owns their restaurant or three restaurants or something like a mature, established business. Given the level of debt that you see here, there must be some sort of preconceived notion of stable revenue streams. So how does that -- I mean it seems like a big contrast from the other types of angel and startup and VC-type entities.

MR. KNIGHT: Right. So -- and I think you hit on a good point which is that the purpose of this survey was to try to get a snapshot of the economy as a whole. So everyone from companies that expect to grow significantly, companies that are quite large with up to a billion dollars in revenue to the small, little mom and pop shops.

I mean our view was that there's a lot of interest, there's a lot of focus on potentially high-growth companies, and there's good reasons as to why. But there are also a lot of companies that are maybe flying under people's radar because they're smaller companies, they don't necessarily have a clear path to exit or clear goal to significant expansion, but they still -- they hire people, they provide a living, they provide a value to the community.

In terms of funding near-term expansion plans, the use of cash on hand actually increased the larger a firm was, which makes sense. They're more likely to have cash on hand. We then asked them in the next three years what do you expect. Most -- the largest group, 40 percent, did not expect to raise capital. Now whether that's optimism that they're not going got need to or pessimism that they won't be able to is unclear.

The next largest group, of course, was loan from a bank, non-bank lender, retain funds, debt investment, family offer -- and then one interesting thing is that debt investment from family and friends and equity investment from family and friends actually did a little bit better forward-looking than they did rearward-looking. So I don't know if that is more interest in accessing securities market or what, but there's a slight uptick there relative to what they had done in the past.

In terms of the factors -- and I think this is really some of the most interesting and potentially relevant information that came out of the study. When companies are looking at how they're going to get financing, just generally, obviously the interest rate, the cost of funding is very important to a majority of them and extremely important. The largest sort of component of extreme importance is the cost. But then it's ease, speed and certainty.

Things like knowledge and expertise of the industry from the funder, which of course would be relevant on more or an equity angel investment side, important but not critical; tax advantages, important but not critical; diversification of funding source is apparently not that important. Really it's how much am I going to pay for this money, how quickly am I going to get it, how certain is it that I'm going to get it, how easy is it for me to get it.

When using -- when looking at non-banks for financing, again, you had better interest rate, ease of access, certainty and speed. What you saw Is that while a better interest rate was very -- was obviously important, this seemed to be -- the ease, speed and certainty seemed to also become important. But then if you look down at the bottom, the funding and asset project matching, all of the sudden, that is not the most important thing to them, but it has an importance to a large group of them, and I suspect that's because they're looking at specialty funding. If you're not going -- you're not going to sort of a general bank, you may be looking at specialty funding, and so you want something that matches your special need.

We asked: Do you think that non-bank sources of funding are superior or inferior to banks? And frankly I'll admit that when I saw this I was surprised. It's almost a 33-33-33 split. Banks are -- 37 percent consider banks to be superior to non-banks, but 35 percent don't know, and 28 percent don't think that they're superior.

MR. NELSON: When you actually talk about nontraditional lenders, is that banks versus credit cards versus someone who might loan me money? Can you talk about those distinctions a little bit?

MR. KNIGHT: So nontraditional lenders are non-bank business lenders, not credit cards, generally issued by a bank, but things like I mean a marketplace lender, a specialty finance, cash -- emerging cash advance, any -- and it is sort of a big pot I will admit, but that sort of non-bank specialty small business lending. Uh-oh.

DR. BAUGUESS: While they're working on

technical challenges, with respect to the banks, is --
are these community banks, local banks, bigger banks?
MR. KNIGHT: All banks.
DR. BAUGUESS: All banks.
MR. KNIGHT: All banks.
DR. BAUGUESS: Is there a local nature of the financing for these smaller loans that it's more likely for a small bank to loan to small business than to go to a national bank?
MR. KNIGHT: Well, our survey did not ask into that. I do think that there's some good information out there, but that was not the focus of our survey.
This other part I think is particularly interesting is that the larger a bank -- or the larger a company is, the more they like banks and the less they like non-banks, which I think makes a ton of sense because of course the larger a company is, they're probably more likely to get a bank loan on terms they like, they're more likely to have a longstanding relationship with a bank.
Whereas the smaller a company is, the less likely it is they're going to be able to get a bank loan on terms they like or at all and the more they may need a different -- which is another thing that came out of this is that the smaller companies are more interested in

getting a quick -- money quickly, get money with certainty, get money easily. Whereas the larger institutions deprioritized that relatively speaking and looked more at the raw cost of the funds.

We asked them why would they take -- why would they consider borrowing from a bank, and overwhelmingly it's their strong previous relationship with their bank. It's not that taking on additional debt is better than other options including selling equity in their company. It's not that the terms are superior. It's that they know and like and have a relationship with their bank.

That -- the strong consideration element is relatively consistent across revenue bands. The taking additional debt is better than other options ticked up generally speaking the larger or the more revenue a firm had. These firms' perceptions of borrowing costs, generally they felt like they could borrow around the prevailing rate. About a quarter of them thought they were borrowing below the prevailing rate, 7 percent above.

MS. YAMANAKA: Do you have that broken down by source?

MR. KNIGHT: By source of --

MS. YAMANAKA: So meaning that the people who thought they were getting a deal, below market rate, was that because of friends and family or was that across all lending sources?

MR. KNIGHT: Unfortunately we did not have that -- I should preface by saying that our survey firm told us that we were really limited to about 30 questions or people are just going to bounce off. And this was a broad survey, so that's something that we wish we could have gone down on and hopefully on a follow-up we can dive into that.

In terms of right amount of debt for the company, almost half believe that there should be no debt. Another almost half wanted to keep it under 20 percent. 7 percent thought around 50 percent was appropriate, and no one wanted to be highly leveraged.

MR. YADLEY: Brian, did any of your questions go to when people were borrowing whether there was -- were enhancements like equity kickers or anything like that?

MR. KNIGHT: No, we did not go that deeply. We felt that that might be a little bit difficult to convey in the type of survey we were running. But it's a good question.

In terms of debt strategy, 56 percent of businesses had a conscious debt strategy. Those tended to be the larger businesses. But almost none of them really didn't -- or almost have of them didn't have a strategy.

The driving -- the drivers for debt levels, why are people accessing debt. The -- 26 percent had no debt. Another 26 percent said that they borrowed when needed, that their capital structure was driven by past decisions. And I think that this is important.

My suspicion is that this is important going back to that bank relationship and bank superiority question, which is if you're not constantly accessing your bank, you have to -- when you run out of money, when you need money, when you want to do something you go and you get a loan. And if the last time the bank said yes and you felt pretty comfortable with that, you're going to have -- and particularly if you also have other products with that bank, your bank checking account, your bank credit card or your corporate credit card, et cetera, you're going to have a strong relationship with your bank.

Now if the next time you go in the future, which you don't know yet, they say no, that may impact your relationship with your bank, that may impact your perception of how good bank funding versus non-bank funding is.

MS. TIERNEY: Brian.

MR. KNIGHT: Yes.

MS. TIERNEY: One of the things that I would like to know -- like you were talking about doing some follow-up with this, but you also need to maybe look at a lot of these businesses, the first thing they're doing, oh, money, oh, I need to talk to my banker. And I know you said in here a lot of it is because maybe those businesses don't understand VCs, they don't understand some of the other types of markets they could utilize, but sometimes it's beyond them understanding and their influencers and getting the information out to the bankers. Because you think of a tax implication, oh, I'm going to go to my CPA.

You don't think of, oh, I'm going to look at SEC filings or paperwork and so I think that's one thing that would be good to take into consideration, that maybe it's not so much that they didn't know, but their expert that they refer to for ease -- because I've seen other federal agencies get a bad rap for, oh, well, this one said no because when they talk about regulations, well, it wasn't truly the regulation. It was that entity not wanting to fill out the paperwork, that banker maybe not being as familiar with the process, just as a side note.

MR. KNIGHT: Yeah, that's a good point. And I will say I omitted from this slide -- it's contained in the report, but we did have some questions about the SBA. Almost no one used the SBA, no one liked the SBA and they found it to be -- which is no knock against the SBA. I think I saw Nate against the SBA here somewhere. But they found the process to be burdensome, cumbersome, time consuming, difficult, and so they kind of -- a lot of them bounced off that and went to go do something else.

MS. YAMANAKA: And I have a lot of experience in that and especially during the last couple years of the SBA. Frankly, they have improved their processing and their servicing client relationships for lack of better words. But I think to your point, Lisa (sic), is that if the intermediaries in the sense that the bankers are not familiar with it, they're CPAs, the people who are going to be the experts at presenting options, it's not going to come up.

So I -- even -- it's -- you've got to get past the barriers, the gatekeepers because business owners are not experts in the SEC, in banking relationships, in tax or anything. They look to their cadre of people and if they don't know or if it doesn't come up or if -- sometimes I have to really talk clients into things because they don't want to take on debt or they don't want to pursue alternatives. They go with what they're familiar with and what their peer group is, too.

So if they hear somebody -- that's why banking is tremendous. If a bank were -- develops a reputation as having a particular specialty in an industry, which will allow you theoretically greater latitude, then all those industries group in that area. So I think there's some nuances in here that are not otherwise --

MS. YADLEY: I think another thing may be -- and I don't know if you found this to be true -- going to a bank -- because I think you're right, Lisa (sic). People don't know about all these other lenders. But banks, even some relatively small banks under 20 billion, are offering a lot of services.

So people call their bank, they're not just getting a line of credit. They have all kinds of specialized finance groups, they have equity relationships, and so I think for a lot of the companies probably at the higher end of your range of companies, going to the bank doesn't mean the same thing as when you're at the lower end and you're really going to the bank for a loan.

MR. KNIGHT: I think -- my suspicion is that that is absolutely true. I mean this survey, which, again, was meant to be sort of a high-level snapshot, that does seem to vie with the information regarding how the larger a company is, the fonder they were of their bank, the better they thought of the bank and bank financing versus a small company, and that seems to jive with other evidence out there that the danger is that banks are retrenching from the smallest of the small.

The big companies, banks are still more than happy to work with them, it makes sense, the regulators are happy with it because it doesn't pose a significant credit risk, it's profitable. Whereas a smaller institution or a smaller company looking for a smaller loan is riskier and the underwriting costs for a small loan are not that much different from the underwriting costs on a big loan. So you run that risk.

In terms of debt-to-asset ratio, the smaller firms tended to be zero to five. Larger firms tend to have a higher debt-to-asset ratio. Smaller firms, not surprisingly, tended to have under a half million in debt. Larger firms tended to have -- like the larger firms, the majority had over a half million in debt. Some of them didn't know how much debt they had. So make of that what you will.

And going back to the earlier conversation about awareness of nontraditional sources of capital, and let me preface this by saying this survey is about a year old, things have hopefully improved somewhat. But there was relatively little awareness on the part of firms of alternative sources of capital, private equity being the most well-known. Of course we split out private equity, venture capital, angel investors, peer-to-peer loans.

So -- and I will say in the report we do preface by saying we trusted people to use their judgment in terms of language. It was hard to control for that. So you may want to lump private equity, venture capital, angel investors all together, but obviously some people viewed them differently.

DR. BAUGUESS: What was the question? Do you know this exists and what it is? Or was it do you know how to get it if you wanted to pursue it.

MR. KNIGHT: It's are you aware of it. And so --

DR. BAUGUESS: So 70 -- three-quarters of the population didn't know what peer-to-peer lending was?

MR. KNIGHT: Apparently so.

MS. YAMANAKA: I'm not surprised at all. That is -- if you look at the broad spectrum, there's a huge number of businesses out there that they have their eye on their widget and their service. And that's -- maybe they've been around for a long time. They are just looking at how to do what they know how to do. Everything else they think is for -- or they all know -- they say, ah, that's just Silicon Valley, oh, that's what we get -- oh, that's just a tech. I'm an old-fashioned manufacturer. A very high-tech manufacturer, but they think that all the private equity and venture capital -- they don't even want to talk to you about it. They know their banks, they've always delivered, they know the game, they know the rules.

If I do this -- average -- if I produce this, if I've got this cash flow, I know someone's going to fund me. On the other thing, it's a little bit -- it's nebulous because it is about relationships and they haven't established those relationships. Nor do they have a conduit to get them there quickly.

MR. YADLEY: I think that's consistent with your findings, too, Brian, that equity is way down what they want to give and the banks by and large are not asking for --

MR. KNIGHT: Well, and I mean my sense is a lot of these businesses are not good equity candidates. It would not be good for the business, it would not be good for the investor because they're unlikely to have the type of event that makes equity worthwhile.

MR. GRAHAM: So again, Brian -- sorry, I talked over someone. Okay. Again, Brian, there is awareness when you are unaware of a type of source if you will and then there's awareness that has to do with whether or not you understand that these sources are available, but you have no one to contact. I mean you have no idea how to tap into it. Do your numbers cover both?

MR. KNIGHT: So the -- the most honest answer is I don't know because the question is are you aware of this sources of capital. So what was in the mind of the respondent when they said, like, I've never heard of this before or I know vaguely that this exists, but I have no idea if it would be appropriate for me, there may be some conflation there. But we don't -- so I can't -- we don't have a question that teases that out. So di ton know --

MR. GRAHAM: Yeah, this kind of goes back to outreach, which I think -- assumption that we should kind of focus on as a committee.

Xavier.

MR. GUTIERREZ: I was just going to ask a quick question. Is there a goal, Brian, of doing this survey again post-all of the kind of growth in the marketplace lender space, and in particular because of the fact that you now have very large money center regional banks that are starting to utilize those platforms for small dollar amount lending, basically offloading anything sub-a million dollars to those platforms and whether or not one awareness is increasing as a result?

And two, as a bank owner, we're actually seeing a reaction against that because of the fact that while ease and certainty kind of is there, the additional services that go beyond just the capital are obviously lacking. And so there may actually be a retrenchment back to not just community banks but to credit unions as well, which is also another factor that I don't think has been included in this. So it's a long-winded way of asking: Are you guys going to redo it given the growth over the last 12 months in marketplace lending?

MR. KNIGHT: I certainly hope that there is an update to this survey. I haven't talked to my colleagues at the National Center for the Middle Market, but I definitely think -- I agree with you. I think there would be value to it.

And like I said, I mean, some of this information I hope is stale because -- and we're going to get to a couple more slides here where there is relatively little understanding of some of the JOBS Act-related changes and it's my hope that that has improved over time, particularly as these have come online -- these regulations have in fact come online.

DR. BAUGUESS: I just wanted to echo -- I mean it's a great idea. Just from the SEC perspective when we do our economic analysis, this is the type of information issuers search. Costs and knowing where to get capital we have a really hard time measuring. We don't have a way to get this type of information. The extent that you repeat this and show us change, maybe even alter the questions to ask specifically about new exemptions would be extremely valuable information to have.

MR. KNIGHT: Sure.

MR. REARDON: Sebastian, is this an opportunity for your group to maybe put some educational information on your part of the website that says if your banks turn you down, these are the other sources you go to? I mean the risk you run is that each one of these groups won't like what you write about them.

But it seems to me that that might be something that's useful even if you just link to somebody else's narrative; if you're interested in venture capital, go to this industry link or something like that. But for somebody who just doesn't know what to do with a small business, and I agree those people don't know, maybe that's something that's not too hard to do and it's helpful.

MR. GRAHAM: I think it would be helpful, and that's what I was getting at when I mentioned outreach. I mean it seems to me that there's an education component, and I know that that's one of the things that we certainly are kind of required to focus on through the

JOBS Act and perhaps other areas as well, but it seems to me that not only is -- are we lacking in terms of -- or that we could do more in terms of outreach to issuers. I think we could probably do more in terms of figuring out how to partner with sources as well.

There is -- there are foundations in other organizations where I think they are sources of capital that people don't fully appreciate. And for that matter, you think about industry groups as well. So I think that there's -- I think this is an important area, and it is something that I think would -- it would be good if we focus on it a little bit and maybe came up with some ideas.

MR. GOMEZ: I think it would be extremely helpful for the committee to focus on it and especially tee up potential ideas of how best to reach to people. One of the things that we have been doing over the past year and I expect not only will continue but will increase now that the rules -- the major rulemaking in the JOBS Act has been finalized is the SEC partner with the SBA in order to actually reach out to different locations throughout the country. Part of the goal is not necessarily go to the stereotypical location where you expect you are going to find companies or development, but also reach out to other areas that are not the traditionally sought after places. So nothing against Boston, but let's think about is there places to go other than Boston, other than the Silicon Valley where we can also do outreach to groups that are interested in funding.

The one thing that I think that's a very interesting topic for the committee to take up is I personally what I find to be one of the most challenging aspects of the outreach is when we go to some of these events, there's a lot of interest from people in learning about it. And then the next logical question that comes up is: Look, I have this great idea and you just talked about crowdfunding, you talked about Reg A, you talked about this thing called 4(a)(2), and I have no idea which one is the right one for me. Can you tell me which one is right for me? And that is not something that the SEC can provide as far as that guidance.

So I think one of the things that would be very important for -- to hear from the committee is not only what the outreach strategy should be try to get the best bang for the buck as we are using our limited resources to try to provide the message, but also how do we go through that gap of this is what the rules are, but at the same time we're not your lawyers, and we can't serve as your lawyers or advisors. How do we cross that gap so that they're actually able to not only get the information about what the exemptions that are available, but also what is the best one for that one company, which of course will vary tremendously based on the type of company and the situation in which they're at.

MR. NELSON: I also think that one of the side effects of the ban on general solicitation has been it's been almost illegal for me to tell people that I'm raising capital for my business up until a couple years ago. And so because of that, the only people who generally know how to raise capital for a business are accredited investors who are rich by definition.

So people who are not rich do not know that being an angel is a thing. They probably don't know angels or they don't know that people are angels that they know. And so I think there's been this unintended consequence in the general solicitation thing where how do I start my business, credit card or I take a second mortgage out of my house. The banks, no, they're not going give me any money because I'm not profitable.

And the frequent complaint that I hear about entrepreneurs and one of the reason why people come to Silicon Valley to raise capital is because the general consensus around the world is that it's one of the few places where there actually is a market for small stock equity, which I think if we can try to fix some of these problems and make people more aware, we move the economy, which I think is pretty awesome.

MR. GRAHAM: Catherine.

MS. MOTT: I think Sebastian's comment about partnering with the SBA makes sense. And because it's the one place that would make sense for everyone to go to it and provide a consistent message and can deliver that message to all its communities. One of the things I will tell you in Pittsburgh, that we have a very, very proactive innovation-focused mayor.

And he created an innovation office. And it's a one-stop shop where you can go and say I need an incubator. Well, there's 20 incubators in town. I'm trying to get some NIH money. Here's some suggestions for you to go get and to try to apply for NIH money. So there's a one-stop source there that provides a lot of information.

I have seen in other communities -- this is not trying to slap the SBDC on the hands, but SBDC in another community which we are very active in where SBDC tells all of the incubators is you don't need them, you just need us. So it's -- there's even a lack of understanding among the things that are partnering with SBA. So if we can start with a general message with the SBA and kind of filter it into the -- all of the components that integrate with the SBA, I think it might be a good start.

MR. REARDON: Could I add to that that I think the focus, if I don't know what venture capital is, the starting point is probably not the SEC rules. The starting point is probably the forest and what is venture capital. And perhaps even the way to do this is through videos because so few people read anymore. They want -- we get -- I've got a face for radio, so I wouldn't be the right person. But get somebody to do it via talking --

MR. GRAHAM: I don't know, Patrick. I kind of see you as --

MR. REARDON: No, you'd be much better. You'd be much better. And somebody do a video of your bank just turned you down. Well, we're going to tell you the five options or six options you've got and each one of these is 10 minutes long and then there's more material you can get if you want to read on it.

But I think if we start with -- well, a relative of mine just got an award for outstanding performance because she took a company's website and focused it from what the company wanted to what the customer wanted. And here you've got to say what does my customer need. And my customer needs you to hold their hand and say here are the next steps for you, and by the way, go get a lawyer who knows how to do all this stuff because it's complicated.

MR. GOMEZ: And, Patrick, I think we have the perfect cast here for those videos because we have members of all of those different groups. So we have angel investors, we have bankers. So maybe that's what we need to do and actually take a little bit more of your time and actually have you record those videos.

MR. GUTIERREZ: In all seriousness, this has been an issue that we talk a lot about, which is this continuum of capital, right? So -- and trying to educate people that what works today may not work for them tomorrow, and by the way, you might not even know what works for you today. And so as we think about this, I'd like to encourage sort of that understanding.

Obviously, the SEC sits in one particular aspect of that continuum, but it's not in a vacuum. Right? And so I wanted to highlight that. I also wanted to reiterate the point that it is very, very important to educate the service providers of those companies. Because at the end of the day, a small business is really interested in making it, right, making payroll, continuing to be profitable. They turn to their lawyer, they turn to their accountant, and so really when you talk about nontraditional platforms to go to, you'd be surprised how much education can actually get done by going though those enterprises across this continuum of capital. So --

MR. GRAHAM: Thank you for that.

Brian, we're going to let you finish.

MR. KNIGHT: Okay. Great. So -- and admittedly this one is I hope one of the staler slides here. Almost 80 percent of firms were unfamiliar with the JOBS Act proposals. Among --

MS. TIERNEY: Does that go back to the idea that before that a lot of the companies in the survey are not the type of companies that would use equity to raise capital, or do you think it's a different issue?

MR. KNIGHT: So this is familiarity, so that's more general. We -- among those who were familiar, about 90 percent at the time said that they would not consider using one of these JOBS Act proposals. Among those who said they would -- and admittedly this is a small sample. The biggest reason was that they thought it would be good public relations or followed by thinking it would be -- provide better terms or be less expensive. Only about a quarter of those who were interested thought that they wanted to expand their investor base.

Among those who were -- would be hesitant or unwilling to use the new methods, the biggest reason was that they didn't know enough to feel comfortable, which of course makes sense and followed by uncertainty, so we can lump those together. Potential for fraud, and then they wanted to know their investors, which I think has been a recurring theme about the value add -- potential value add to investors, particularly on the equity side.

We asked if they were listed on a stock exchange. Only 3 percent said they were currently listed. 2 percent said they didn't know, so whatever. 92 percent said that they have not considered listing, and 3 percent have considered it but haven't done it yet. Surveys. Okay.

So biggest barrier to the companies of as to why they wouldn't do it, the biggest one was that they were just too small to consider going public, followed by cost, regulation, and then lack of liquidity. So these are themes that have been echoed again and again and again. One, the private -- or the public markets are not really a good option for a significant chunk of companies.

That's just not -- to your continuum of capital point, in that continuum of capital, I think it's very fair to say that there are multiple forks in that road. And so trying to -- we can fix and improve certain areas, and that will help with the companies that will travel down that path and not necessarily help any of the other companies, and that's something that people should be mindful of.

And then I guess to sort of get to why any of this matters in terms of expansion plans, 54 percent said that their expansion plans would not change in response to an increase of cost and capital. 28 percent said it would only respond to a significant interest rate swing, and 18 percent said that they were highly sensitive to changes in cost and capital.

And then if you look, if we broke it down by revenue band and the largest groups say it would not change, where the smaller companies, the up to about $2 and a half million in revenue companies -- and my suspicious is those are in a grow-or-die mode, we have to do it, so we're going to do it. But then the other side -- on the other side, the smallest companies were also relatively speaking the most sensitive to changes. And I guess those are companies that are not in a grow-or-die mode, but also don't have a lot of leeway in terms of the money that they can raise.

That -- so that's the presentation. I'm, if there are any additional questions, happy to answer them or try to anyway.

MR. GRAHAM: Thank you, Brian. So open it back up for questions.

Greg.

MR. YADLEY: Not a question so much, but I like Sebastian's comment about the SEC's not the lawyer, so you can feel free to give them Stephen's and my Texas colleague's and my names anytime you want. But that is not the primary goal of the lawyer, although that is part of our counseling. One of the themes that's come up is that people don't understand who these alternative capital sources are. If they do, they don't distinguish among them.

Another tool in the arsenal, which obviously our committee has talked about in the past, is private placement brokers, somebody who may know you want this kind of capital source, or I know these 10 people, and really the goal is not to sell their capital or their sponsored fund, but to match a source. So I hope that's something we'll continue to talk about at our future meetings.

MR. GRAHAM: Okay.

MS. HANKS: Yeah, I certainly just wanted to echo what Greg said about we need to get the finders thing fixed. This term of this committee, that should be one of our objectives. Do or die. The other thing I just wanted to mention, carrying on from the banking issue, there are some jurisdictions, UK being one of them, where rules are being instituted for banks when banks turn down a small business loan application. They're required to say, well, we're not going to give you anything, but here's another source.

Now that's a difficult thing to dictate when you have 16 different banking jurisdictions, banking authorities and then 50 different state ones, but there might be something like that we could do on a voluntary basis. And I have talked to some local banks who might be interested in saying, well, you're too early for us, but here, here's a crowdfunding platform.

MR. KNIGHT: If I might put one bug in the committee's ear, and we've submitted a comment letter touching on this, one of the things that struck me when I looked at this data is just how interested people were in debt as an option. And I think it's worth considering whether like the private offerings -- whether or not they are well suited to debt offerings and whether the structures and requirements around these private offerings, many of which are built for either equity or debt, or are capable of using either equity or debt, whether or not there's any profitable way to -- if you were to create a debt-specific offering, whether you could do it with sufficient and appropriate consumer protection or investor protection while creating a lower barrier because of the unique nature of debt. And so my suspicion is that there might be that possibility, and that might be something that's at least worth contemplating going forward.

MR. GRAHAM: And that's -- you're talking about pure debt as opposed to convertible debt?

MR. KNIGHT: Pure, simple, vanilla debt. Basically something that functionally competes with a bank loan because that seems to be where most of the demand is. And to the extent that banks are retrenching, there may be an unmet or unfulfilled need. And not that this is going to replace banks or replace marketplace lenders or replace anyone else.

It's more to augment the suite of options available because everyone's going to have different needs, wants and options available to them. But if one can be created that works without creating undue risk to investors, that might be a nice thing to have.

MR. GRAHAM: Thank you.

Sebastian, are you going to address this kind of where we are with the finder versus broker this afternoon?

MR. GOMEZ: So I'm hopeful that John, who was here this morning, will be available this afternoon in case there's questions from the committee.

MR. GRAHAM: Kind of find out where we are. Okay. Any more questions before we break for lunch? Okay. Then let's break for lunch.

(Whereupon, at 12:36 p.m. a brief luncheon recess was taken.)

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

MR. GRAHAM: Okay. First we need to turn to a bit of housekeeping. I don't know if you have copies. But -- okay. Generally, we pass out -- well, we'll be passing out current copies of the bylaws for your information and for your future reference I guess.

The current bylaws of the committee were adopted when the committee was formed in 2011. When the committee was renewed by the Commission in 2015, there was a change to the charter, which now states that the members are appointed to serve essentially by the Commission, and they will serve at the pleasure of the Commission.

The original bylaws provided that the committee was to be appointed by the chair of the Commission. So that change was made. The committee has reconstituted with the Commission as a whole providing greater input, and that's kind of the current fact of life.

And so it's time to amend our bylaws so they kind of conform with the reality of the current charter. So what we need to do is remove three words: chair of the. And that's it.

PARTICIPANT: So moved.

MR. GRAHAM: Thank you. All right. Does anyone want to talk about this? All right. So all those in favor?

(Chorus of ayes.)

MR. GRAHAM: All those opposed? All right. We have amended our bylaws.

Sebastian, will you provide the committee with an update on the current status of rulemaking and other initiatives at the Commission?

MR. GOMEZ: Sure. Happy to do it, and in many ways the presentations this morning, especially by Scott, cover a lot of the stuff that I was going to cover. So I encourage you guys to chime in if you have questions or if you have insight as to what you are seeing in the different areas that I'll touch upon.

So let me start by noting again that last year the Commission finished all of the major rulemaking under the JOBS Act. I had a section here where I was going to talk about what we're seeing in the context of Reg A offerings, but Scott stole my thunder and did it much better than I could have done it and provided even more data than I could have provided for you.

So I wasn't going to spend a whole lot of time on Reg A unless you guys had some thoughts or some insight as to what you've seen or you experience there.

MR. HAHN: I was going to say earlier, so we went public in January of 2014, but in 2012 and early 2013, we were in a position where our lead compound was in a phase 2 and we needed further funding. So we didn't have the data yet to access the public markets for an IPO. So we were looking at a lot of different avenues, and Reg A popped up. At the time it was only a $5 million limit on that.

The 50 million Reg A+ would have been perfect for us at that point because it would have given us an opportunity to raise the money. The challenge with the IPO was that we had to spend $2 and a half million on lawyers, accountants and not knowing if we were actually going to be able to close a deal.

I do think the one challenge, though, going forward, though, is liquidity issue on the markets on the back end. On the private side, I think the way that before Reg A+ this was addressed is a lot of the public investors will, in the last several years in the biotech area, have started making investments in private companies. But they call those crossover rounds. And a lot of the deal terms are structured whereas they'll do the crossover round in the company, but there are certain stipulations in the agreement that says if they don't go public within the next 12 to 18 months, the crossover investors will get more of the company.

So I think Reg A+ is -- it's great, it's another tool in the toolbox to help companies in that type of position raise money. But I do -- there is -- we're going to have to take a look at the liquidity side and, yeah, there are some other conversations about other markets for these securities before they're actually public.

MS. HANKS: If I could just say something about the implementation of Reg A, we've done six separate filings. We've done filings for six separate companies and gotten nine rounds of comments, and they were uniformly useful, helpful, not nitpicky. When we have a foot fault of like how we've not quite filed something right in part one, nobody picks us up on it.

They call us and say we think you might like to amend that they don't even say and you should have known that, Sara. And so it's been terrifically helpful. And so the implementation is great.

I absolutely second the stuff about the

liquidity. That's going to be a huge, huge, huge thing for the investors. But one thing that when you look at the adopting release and the assumptions that DERA made about who would be using this, I think that the fact that there is a whole load of pre-revenue companies using tier two, and that's something I think possibly that the commission wasn't expecting. But you're probably going to see a lot more of those.

MR. GOMEZ: Thank you. Thank you for all those thoughts. I've -- I did not introduce Joanne Rutkowski. Joanne is in the Division of Trading and Markets. And I was reminded by this because I was going to jump into crowdfunding next. But Julie within the Division of Corporation Finance and Joanne within the Division of Trading and Markets work on the team that implemented the rules that resulted in Regulation Crowdfunding.

And when I say this, I really mean it. It was a very challenging project for us at the staff. On the one hand, it was complex because we were creating a brand new exemption in the 33 Act. But also our colleagues in TM with respect to the 34 Act, there's a whole new framework for intermediaries that are registering as funding portals. So it was a very challenging project. We did benefit from a lot of comment in that area, which was very helpful, and we are eager to see how it will work out.

Just to give you an update on -- as you heard this morning, the rules are not yet effective. Funding portals have been able to register starting in January and the chair mentioned that we've already seen some of them starting to submit the form to register with the SEC.

For issuers, as it was noted, the rules will go into effect on May 19th. And although the issuers can't currently file a form until that date, they will not be able to file a form to actually do an offering. We did open up the ability for issuers to test file, to have access to what the form would look like and access the system .

We issued a press release on December 18th providing information as to how an issuer would go through the process of testing the Form C. And the reason we did this was two-fold. On the one hand we are coming up with a new form that gets submitted via EDGAR. And whenever you're dealing with a new form, there can always be technical challenges. And the one thing that we noted in the release and we were hoping is that as people test the form to the extent that there were problems with the form, they could let us know so that we can address those before the effectiveness.

The second reason for it is the scenario where we are going to have issuers that are likely not familiar with the process of filing something with the SEC. So the idea of opening it up for them to test the form, it also gives them the ability to actually see what they're going to have to go through and what the form looks like so that when it comes May 16th, they are more informed as to what the process will be like.

For any of those watching and interested in this, the -- as I mentioned, the instructions are on a press release on the Division of Corporation Finance portion of the website as to how to do it. And unfortunately you have to move quick because we opened up the testing December 18th, but it closes at the end of this month in order to give us sufficient time to put in place all of the changes that have been suggested to us and fixes to the system.

So with that, I was going to turn to a quick update on Rule 147 and 504. You heard quite a bit bao9but both of those in the morning. The same day that the Commission adopted final rules with respect to Regulation Crowdfunding, the Commission proposed changes to Rule 147 and 504. I know a lot of people have talked about Rule 147, 504.

Sometimes we -- here at the SEC, we run the risk of talking so much about rules and we don't actually explain what they do. So in many ways, Rule 147 is a rule that is -- as was mentioned this morning, was adopted by the Commission in 1974, and it's a safe harbor under Section 3(a)(11) of the Securities Act. And it's known as the intrastate exemption.

The idea of Rule 147 in Section 3(a)(11), the concept behind it is that if you are conducting an offering, if you're an issuer in a specific -- doing business in a specific state and you're conducting an offering and selling -- both offering and selling only to residents of that state, then you don't have to go through a process at the federal level. You only comply with the requirements at the state level itself.

There is no limitation under the federal rules as to how much an issuer can raise pursuant to Section 3(a)(11) or Rule 147. Although, at the state level, there could be -- and many states, in fact, do have requirements as to how much can be raised pursuant to the intrastate exemption in that specific state.

Rule 504, just very briefly, when people talk about Regulation D, mostly people are focusing on 506(b) and (c). Rule 504 is also part of Regulation D, as -- historically has been known as the seat capital exemption. And currently it allows an issuer to raise up to $1 million over a 12-month period.

So why did the Commission propose amendments to Rule 147 and Rule 504? We've heard from this committee, we've heard from other commenters, and we worked very closely with Mike and his colleagues at NASAA. And what we heard is that specifically with respect to Rule 147, this concept of limiting both the offer and the sale to residents of a particular state was somewhat outdated and difficult to implement, especially in an internet age when you are trying to post your offering on the internet and it's hard to limit how that offer is made only to residents of a particular state, because as all of you know the internet doesn't really know that you crossed the boundary between one state and another.

So the -- these concerns led the -- and additional developments in technology and communications led us to believe that there was perhaps a need to modernize that rule.

So what did the Commission specifically propose? The Commission proposed creating a new exemption from registration that would be Rule 147. Instead of being a safe harbor, it would now be a new exemption under the Securities Act that would permit offerings to take part with respect to any person so long as the sales were limited to residents of the same state in which the issuer is doing business. So you are no longer limiting the offer aspect of it, but like the current intrastate exemption, you continue to limit those who purchase to residents of the same state in which the issue is doing business.

The rule would also ease some of the other requirements that exist in Rule 147 that would make it available to a greater number of issuers to take advantage of the rule.

The proposed amendments would limit the ability of the new exemption to issuers that are either registering the offering in state or issuers that are making an offering under state law pursuant to an exemption that limits the maximum amount that that issuer could raise to no more than 5 million over a 12-month period and that the state exemption also would have to impose investment limitations, although it did not mandate any specific investment limitations.

With respect to Rule 504, the proposal from the Commission would raise the $1 million limit, which, by the way, was set in 1988 and had not been changed since then to $5 million and would also disqualify certain bad actors for participating in Rule 504. The increase in the aggregate offering amount would facilitate small companies' ability to raise capital and also provide greater flexibility for states to actually come up with coordinated review programs, regional coordinated review programs as the maximum amount that could be offered and sold would increase from 1 million to 5 million. The bad actor disqualification is substantially similar to the bad actor disqualification that applies to the other portions of Regulation D. So in many ways it would create consistency across Reg D with respect to who are the bad actors that are not able to participate.

The comment period ended January 12th, although we always welcome comments. And if comments are received after that date, we'll consider them of course. The Commission so far has received 26 comments on the proposed amendments. And commenters generally were supportive of the changes that the Commission proposed, including the amendments that would permit this broad dissemination of offers so long as the purchasers are residents of the same state as where the issuer is doing business.

However, many commenters did recommend that the Commission did not replace the safe harbor in Rule 147 with this brand new exemption, but instead commenters recommended that the Commission include the new exemption in a separate rule and then retain but modernize to the extent possible the safe harbor so that there would still be a safe harbor under Section 3(a)(11).

The final thing that I just wanted to briefly touch upon is the work that the staff has been doing on the accredited investor definition. Dodd-Frank required the Commission to review the accredited investor definition as it applies to natural persons. And Chair White instructed the staff to prepare a report in connection with the first review. Staff primarily form CorpFin and DERA worked on the report, although we did get help from a lot of the other offices and divisions of the SEC. And the Commission published a report on December 18th that is available on our website.

As many of you know and you've heard so far, the accredited investor definition is a keystone of Regulation D. And when it comes to natural persons, the definition relies on two types of thresholds.

Accredited investors under the current rules would be an individual who has an income of more than $200,000 over the last two years and an expectation that they will have an income would exceed that threshold in the current year. And with respect to individuals who are pooling their income with their spouse, it has to be a joint income that exceeds $300,000.

The other threshold that is used to qualify as an accredited investor would be for individuals that have a net worth, excluding their primary residence, of more than $1 million.

The thresholds were primarily set in 1982. The 200,000 and the $1 million. The 300,000 joint income threshold came in in 1988, and the taking out the primary residence happened in 2011. There's been a lot of talk about the accredited investor thresholds and the accredited investor definition because they have not been updated for inflation since the 1980s. The 200,000 would be approximately 500,000 today, the 300,000 approximately 600,000, and the $1 million approximately $2.5 million today.

So the staff put together this report that considers a number of recommendations that have received -- they've received recommendations from this committee, they've received recommendations from the Investor Advisory Committee, and they had already received a lot of public comment with respect to the definition itself.

So the report not only provides recommendations, but it also sets forth an analysis of what the impact that those recommendations could have on the accredited investor pool.

And so to give you a flavor for what the staff recommended, the staff recommended that the Commission could leave the current income and net worth thresholds as they are now in place, but subject them to -- those investors to a 10 percent limitation. The idea here would be that the amount that an investor could invest in any one issuer would be limited, but investors at the current thresholds would be able to continue to qualify as accredited investors.

The staff also recommended creating a new inflation adjusted threshold that would not be subject to this investment limitation, for example a 10 percent limitation. And it could be something along the lines of what the adjusted for inflation numbers would be, around $500,000 for individuals, rounding up about $750,000 for joint income and $2.5 million for net worth.

The staff also recommended additional ways that the Commission could consider for individuals to qualify as accredited investors that are currently not part of the definition. To give you an idea of some of those, many commenters have suggested that they would be supportive of a minimum amount of investments thresholds. So once investors have indicated that they have invested more than a certain amount, then those individuals would qualify as accredited investors even if their net worth or their income doesn't meet the thresholds.

The staff also recommended considering professional credentials to qualify as accredited investors. So for example if you've taken the Series 7 or the Series 65 or the Series 82 examinations, perhaps those examinations could be evidence of investor sophistication because of the subject matter that those examinations cover.

The staff also recommended looking at potentially investor experience. So if an investor had previously participated in 10 prior private securities offerings with respect to different issuers, perhaps that individual has presumably developed the knowledge and has done the due diligence and understand valuations, things that they've learned through the process of investing in those 10 prior offerings.

The staff also considered including knowledgeable employees of private funds that would qualify as accredited investors with respect to the investments in those employer funds. The idea there is that these employees would have significant investing experience or would have sufficient access to the information since they are working for the funds in which they're actually investing in.

And then finally the last thing I was going to mention -- and the report goes through a number of suggestions also with respect to non-natural persons, as to how the Commission could expand the definition or revise the definition. But the last thing I wanted to mention is there's a lot of talk about the possibility of an accredited investor examination and the staff recommended that the Commission could explore the possibility of designing such an accredited investor examination. The idea of this approach would be to enable financially sophisticated individuals to qualify as accredited investors regardless of their wealth or education by actually proactively demonstrating that they can pass an examination that in many ways would look at their sophistication when it comes to investing in private offerings.

So the last thing I leave you with is what would be the impact of some of these recommendations. If the Commission were to only adjust for inflation, the current thresholds, the current pool of the population that qualifies as accredited investor is approximately 10.1 percent, and that pool will go down to approximately 3.6 percent.

If, on the other hand, the Commission were to adjust for inflation but also come up with new threshold levels -- I mean retain the current threshold levels but impose a 10 percent limitation plus also come up with an investments test, in essence the idea of if you have a certain amount of investments, then you would be able to qualify as an accredited investor, our calculation from our colleagues in DERA will show that the current pool of 10.1 percent would go up to about 11.5 percent.

What these figures don't account for is all the other recommendations that in many ways are not quantifiable to us because a lot of those tests that look at other measures of sophistication, we expect that they would only increase the size of the pool, but we don't have data to quantify how much by how much they would increase the size of the pool.

So I've already taken a lot of your time.

Joanne, I don't know if you wanted to say anything about finders and --

MS. RUTKOWSKI: I guess it's no news is good news on finders. It's really -- I was listening to Sebastian talk about crowdfunding. It reminded me about we always have this tension in the broker-dealer space because the scope of the definition is so broad, and there's so many different types of limited purpose broker-dealers. And that certainly is something that we've been studying and we're trying to develop approaches.

But at the same time, broker-dealers, intermediaries, folks who are playing with other people's money play an important role as gatekeepers. I mean even funding portals in the final rule have a safe harbor that allows them to determine whether and under what conditions to admit -- I'm sorry, issuers to their platform.

So it's a serious endeavor, it's a balancing act, there are some no action letters out there. We did the M&A broker no action letter a few years ago. Paul Anka is still kicking around. FINRA is trying to step up to the plate, I think, with the crowdfunding initiative. They had to revisit the rule book. I know they have out for comment with us the capital acquisition brokers. And there's a March deadline on that.

So I guess the short answer is the staff is continuing to study, but it's not an easy answer.

MR. GRAHAM: Is there any thought of interim steps?

MS. RUTKOWSKI: I think we're open to the full range of possibilities.

MR. YADLEY: Hi, Joanne. I'm usually the voice of reason. And I totally agree with what you said. You weren't hear this morning. We touched on this briefly. There are no easy answers, but I think this committee made recommendations last time and we did have a whole range of ideas to think about. While we may not get to the finish line and there may be differences of viewpoint on this committee, within the staff, at the Commission level, it really doesn't seem to us that we shouldn't do something and propose. Because not that more study wouldn't reveal more nuances, but since the ABA taskforce report in 2005, I think we've pretty much identified 90-plus percent of the issues.

And so just speaking as a member of the committee, I hope that we will move from the study phase to a proposal stage and I think the chairs and the rest of my fellow committee members can weigh in, but I think we are very willing to be a part of that process and be helpful, and our prior recommendations sort of set the table for not just studying but making some recommendations, and I hope you will.

MS. RUTKOWSKI: Thanks, Greg. I appreciate it, and I will take the message back.

MR. REARDON: I deal with this issue regularly. I have small clients. And it's very difficult when somebody shows up with a -- to your client and says I can raise a million dollars for you with my rolodex and they don't have a license. It's very hard to convince your client that this person is probably promising what he or she cannot deliver and in addition is going to get them in trouble for violating the law.

Frankly, I've lost a number of clients over that, over my refusal to be involved with that. And this has been going on for years, and I've spoken to -- who was the head of CorpFin during Mary Shapiro?

PARTICIPANT: Meredith Cross?

MR. REARDON: Yeah, I spoke to her. She put me touch with somebody in the Fort Worth office of the SEC. I talked to her and she said, well, can you give me some names. So I gave a name, somebody who's within the shadow of the building at the SEC's offices in Fort Worth. Nothing ever happened that I saw.

I went back and looked at the Daniel meetings that are held in November that all the studies are on there. And without looking very hard, the furthest back I found was 1997 that a recommendation was made that this be dealt with. Okay? So -- and there have been a multitude of studies. You've written a paper on it. I mean frankly I think it's -- the bar at least has taken this as far as it can be taken. I heard somebody who's on the staff this year told that a lawyer who's interested in this that this person at the SEC would not have time to get to this this year.

First of all, I'd like to meet somebody who's so busy they don't have anything else to do for a year. That's impressive. But I think where -- from my standpoint that this has been studied almost as much as the Torah and the New Testament. And somebody, either the Commission decides they're going to ask on this and get serious about it or don't waste our time on it. Okay? And frankly I'm tired of being your enforcement division on this issue. And there are a lot of crooks out there that are stealing from small business people or wasting their time, and it needs to be dealt with. But no more study is needed.

MS. HANKS: If I could just add to that one again and just to build on what Greg was saying, in addition to -- since the taskforce stuff came out, I mean we now have the whole online capital formation platforms, and I'm seeing all the time the guys who are trying to comply with the law are at a disadvantage with the guys, and it's really not fair to them.

There are some platforms out there totally violating the broker-dealer laws however interpreted, not within any no action letter, because they're like we don't need any stinking no action letters. They're just doing their thing. And they say literally it must be legal, nobody's been arrested for it. I get that quote a lot.

And on the other hand, you've got the companies who are using them. If you're using an unregistered broker-dealer, you now have a rescindable transaction, so they've got a problem. And the good guys have a problem, too, the guys who are saying, well, I went out and I had to study for the Series 7 and it took me a while, but now I've done it. So it's a matter of equity.

MS. RUTKOWSKI: I very much appreciate everything you're saying and I will take it back.

MR. GRAHAM: Any other comments on finders versus brokers? I do think that our recommendation was very complete, that -- I don't know what more we could say, but I think if I remember right, in our recommendation we did talk about the possibility of taking interim steps, understanding that there -- I mean we're here to try to find ways to facilitate capital formation by small businesses.

And I don't know the extent it would help, but intuitively you just have to feel that coming up with a rule that's going to enable the people with the rolodex and not receive transaction-based compensation and all the rest would go a long way toward it helping with the situation that we talked about this morning in terms of trying to let -- trying to educate small businesses as to how they can go about and access capital and educate them and who they might go to. I think maybe we need another study just for that, and I'm only being partially facetious.

I think the important point is that we should be able to do something and I'm fairly confident that even though it might appear to be small that it might prove to be significant.

The accredited investor definition, has everybody seen the report? You should -- if you haven't seen it, you should download it or just put it on your screen and take a look. Yeah, I think that one of the things that we should do as a committee is take a good look at that report and see to what extent there may be other suggestions that we might want to give in addition to the recommendation that we provided last term.

And I know that our member, Patrick, has submitted a letter for one and I think that it probably would make sense for us as a committee to take a look at that report and take the opportunity to weigh in.

Do you have anything else?

MS. MOTT: Stephen?

MR. GRAHAM: Yeah.

MS. MOTT: I'm sorry. I was hoping we would address this. So thank you. And I know that the Angel Capital Association, the public policy committee is about to submit a letter as well. I do think this is important for us to address because it can have a significant impact on the amount of capital -- seed capital that's available for companies to get off the ground. So critically important. I just want to emphasize it is -- your numbers I think are pretty close to the impact that it's going to have on the pool of investors. So important for us to address. Thanks.

MR. NELSON: Just two comments. One is could we actually have that report emailed to us?

MR. GOMEZ: Yes, we'll do that.

MR. NELSON: I'd also just be interested in getting kind of a gut feel from the other members of the committee whether they feel that more -- looser standards or stricter standards need to actually be created? Do we need more investments into small businesses and loosening the pool of available capital or because do we need to actually tighten up because of instances of fraud and that sort of stuff?

I'd be just curious to see where everybody else is. I have -- I hang out with entrepreneurs all the time, so the more capital is available to them, the better. I've seen in maybe 10 years two instances of just outright fraud. But that's just me.

MR. GRAHAM: Yeah, well, it's -- I'll let other people respond. But again, we're faced -- kind of the core issue that we're dealing with, if you will, is removing the barriers to capital formation for small business. And certainly when this committee took up the issue and formulated a recommendation, our sense was kind of just that as far as the points that you're making, and that is that we're dealing with a system that currently works. I don't know what the numbers are. It's somewhere between a trillion and two million and two trillion I guess and as far as magnitude of the market if you will.

MR. NELSON: Could I just interject right there? What I saw in the report when I read it last night wasn't $2 trillion. That was funds and all private capital. But small business was 166 billion of that paper. I could be wrong, but that's what I saw was only 166 billion.

MR. GRAHAM: That could be. Anyway, it's -- however you want to kind of define small business, just kind of looking at the private placement market, it's big. And that is -- we all know that that is written by 506, and I guess in today's lingo, Rule 506(b). And so you've -- you have a market, it's clearly substantial, it's clearly important from the standpoint of our economy and job creation and all the rest. And so why constrict that? Why come up with a set of rules that are going to -- intuitively you would think would hurt that market and hurt the -- and reduce the amount of capital that's available?

Well, one way might be the existence as fraud as you suggest. And certainly one of the things that we have to keep in mind is investor protection. We all kind of understand that. But I'm not really aware of an issue that relates to fraud that can somehow be tied back to those thresholds.

MS. HANKS: I think that's true. If we look at what happened in the presentations to this committee last session where we did have some presentations on the existence of fraud. Yes, there is fraud in the private market sometimes, but it is not driven by where the definition of accredited investor is, and nobody's been able to come up with any evidence that that was the case.

MS. TIERNEY: I think I'd also note the last time that the definition of accredited investor was amended was Dodd Frank. And the investor's primary residence was backed out of the equation of net worth, and that decreased the pool of people who could invest I think at that point from like 9 percent to 7 percent. And that had a big impact on the market just then.

The idea of increasing dollar thresholds in a market where there's no real investor protection issues that anyone can point to with specificity, potentially decrease it to 3.6 just because there's a construct that things should have been adjusted for inflation makes no sense. And I think that everything that we see, especially people who are retail investors and not even accredited investors who get so unhappy that they can't invest in the private company space in 506 already, it just doesn't make sense to go to a more restrictive definition.

MR. GRAHAM: And that's also assuming that the initial numbers were --

MS. TIERNEY: Agree.

MR. GRAHAM: -- too high. I mean maybe -- or too low or something. It assumes that they were correct.

MS. TIERNEY: I'd like to see the numbers drop.

MR. GRAHAM: There's two.

MR. HAUPTMAN: Just to Jonathan's question, I know we're not having a poll here, but that would be three votes here for reducing the standard. I'm not 100 percent convinced that on the whole having an accredited investor standard is useful to begin with provided all parties agree that those who engage in fraudulent activity should have the book thrown at them. Accredited investor standard does not exist in other countries, and things still work out over there as well, other places.

And to protect the investor, protect from fraud, fair enough. Again, that's a prosecution's war.

But I would expand the definition of protection. The way you can help protect me is by letting me invest in a company as I'd like to.

MR. GRAHAM: Catherine.

MS. MOTT: one of the things I want to add for the committee is that when the Angel Capital Association looked at how this is going to impact the angel groups in the United States, it really impacted the middle part of America. It didn't impact LA, it didn't impact Boston or New York. Because 500,000 in New York is like making 250,000 in Cincinnati, Ohio or Pittsburgh, Pennsylvania, whatever. I mean I look at the composite of our local angel group as surgeons who make 300, 350, but if they were living in New York, they would be making 500.

So the decrease is --

(Interruption to proceeding.)

But anyways, it's really -- the economic impact of middle America is going to feel it the most, and that's where it's going to hurt the most. So --

MR. GOMEZ: I just wanted to point out and be clear when I gave the numbers the only adjusting the numbers for inflation actually is not a recommendation in the staff study. But there's been enough discussion about it that I wanted to throw that number out there. The 11.-some percent would be the number if you were to actually do all of the staff recommendations. If you were to only impose a 10 percent limitation, granted the pool would stay the same.

Where a -- I don't know, Catherine, based on your membership, as to whether if you're limiting how much someone can invest by 10 percent, whether that would actually cut the dollar amount or not. I mean I think that's an interesting question.

MS. MOTT: Actually we go through an orientation program with our investors, and we actually recommend that they limit 5 to 10 percent of their net worth. But we also encourage them to spread it across several different companies because it's a risky asset class. So minimum 10, but we encourage you to go to 18 to 25. And actually the data shows -- well, from some of the studies out there, there's still a minimal amount of data out there in the studies.

Once you get up to 36 percent, you even have a better chance of -- but it's -- so we do encourage that, to limit it to that. So -- and we've always encouraged them not to include their residence, even prior to it being promulgated. So I mean it's just -- so, yeah, I hear you, but I'm just -- I get nervous when I see the number 500,000, but -- who will be impacted, so --

MR. GRAHAM: So isn't -- I don't know where I come out on this exactly, but isn't it kind of paternalistic to tell people how much they can invest or not? And is that really what we should be in the business of doing?

MS. MOTT: Yeah, we don't tell them. We advise them.

MS. HANKS: I would say anyone who's been through the Angel Capital Association training program should automatically be admitted as an accredited investor because --

MR. GRAHAM: Good point.

MR. YADLEY: And I guess that's one of the things, getting beyond the inflation adjustments and the numbers, the other thing -- and I think the staff and the staff study are terrific because we all agree that the number, whatever it is, $200,000 a year, a million dollars net worth is just a number. As Steve pointed out, it really hasn't been a problem for decades, so -- but okay, we can quibble about whether that number should be adjusted.

But beyond that, the other ideas for expanding the pool makes perfect sense because we all know that those numbers are just a proxy for people who need less protection than other people. So people that have credentials and background and experience investing or through their education or jobs, I think, again, that's a great way to allow them to be part of America's culture of capitalism and democracy. And we should promote that. And by the way, it will lead to job creation, which we're all in favor of.

MR. GRAHAM: Kyle.

MR. HAUPTMAN: For all the talk of inequality that we hear about these days, it would seem odd to me to have our official policy be that the best investment opportunities are limited by law to the 1 percent. Only they can get the top investment opportunities. And one of the ways that one becomes the 1 percent is via entrepreneurship, which we are also making more difficult for them to do.

We're trying to protect this club -- we're not trying to, but this could be the effect -- protect the 1 percent. Number one, you get the investment opportunities, and number two, no one will be clamoring -- fewer people will be clamoring to join you in that group because their startup idea we're making harder to fund.

MR. GUTIERREZ: I'd like to make a comment. I often say that the issue is not access to capital, but the issue is because there's quite a bit of capital out there. And so I look at it from the perspective of the small business owners. Right? And if we are creating a regime and we are creating a platform whereby we're limiting the capital that exists out there, the ones who are really going to be impacted are going to be those business owners. So I'd like to change the framework of -- this conversation as you've pointed out, Steve, is about capital formation opportunities. And for us to be limiting opportunities I feel is really going against that basic tenet.

The second point I wanted to make is I think dovetailing on something that Kyle mentioned, which is I do believe there's a dubious connection between someone's net worth and their financial sophistication. I know plenty of folks who are financially very successful who quite frankly would be considered unsophisticated investors, and I think it would be a shame if we begin to limit those who are allowed to put their money wherever they'd like to based on what they've already accomplished financially.

MR. GRAHAM: Thanks. Jonathan.

MR. NELSON: One of the things that I'm also sensitive to is having been in kind of public service roles before, when you get it right, no one knows, but if you get it wrong, you're in the newspaper sitting in front of Congress. And that's an awful job. And I thank you guys for your service, because it's amazing what you guys are attempting to do, which is prevent all of America from fraud and create markets.

But I think on this side of the table not being the public servant but someone kind of being out there in industry, I would like to think as a committee how do we communicate very, very strongly that I, for instance, want much more access to capital, and I very much want not to protect investors from themselves, but to truly protect them from fraud. Those are where we want the things, the lines to be drawn.

These are my opinions and not necessarily those of the SEC.

MR. GRAHAM: Well, thank you for that, Jonathan.

Can we move on now? Okay. So at this time I'd like to ask Annemarie to -- with your discussion on what the advisory committee recommended last term with respect to 4(a)(1 1/2) and its codification into 4(a)(7). It's all yours.

MS. TIERNEY: Well, I had the honor of presenting this committee last March, almost a year ago, about what we saw was a market need to create a new exemption in the private company space for resales of securities, which was a codification of a legal construct that's referred to as 4(a)(1 1/2). And at that point there was a bill in Congress that created a new federal exemption.

That bill was signed into law by the President on December 4th of last year, and it basically creates a new safe harbor for resales of private securities. Buyers have to be accredited, and there can't be general solicitation.

There is information requirements, so the exemption is only available to a seller if an issuer consents to provide certain information, including two years of financial statements prepared in accordance with U.S. GAAP or IFRS if it's a foreign company. Information about the company's business, names of their officers and directors, some kind of routine things like the name of the issuer, which I don't think is a problem for most companies, their address, title and class.

The nice thing about the exemption is it gets rid of a lot of noise around 4(a)(1 1/2) that existed in the space where Steve and I and many of you operate, which is private company, kind of later-stage private companies that have a significant employee or former employee base who have trouble getting value for their equity unless they can locate a buyer, sell the underlying common stock to fund the exercise of the options and the income tax consequences.

And what we were seeing was a mixed bag of opinions from different law firms that we were working with where some law firms were very comfortable if somebody used the proceeds of the underlying -- sale of the underlying common to cover the cost.

Some were not comfortable with that, so we were seeing some companies requiring their employees to sign promissory notes or give checks to the company in order to participate in the liquidity program where the options were being exercised. So there's just a lot of noise around the space.

The other thing about 4(a)(1 1/2), since it's a legal construct, it's not actually a safe harbor in the rules. It wasn't -- resales were not preempt under state law, so as an intermediary in the private company space, it was virtually impossible for us as a broker-dealer to help locate buy-side interest.

The state law that deals with broker-dealers says that the bid has to be unsolicited, which is the flip from the primary space where if you're a broker-dealer and you have a preexisting relationship with your clients, you can market primary opportunities as long as the investment is suitable to them. In the secondary space, you can't market opportunities at all. And that just didn't make any sense to us. So 4(a)(7) gets rid of that problem as well by creating preemption.

Securities still under 4(a)(7) are covered securities. And so it's just another tool in the box of shareholders and employees of private companies to allow them to get liquidity for their shares to the extent that the company is willing to provide the information. So we're really excited about it.

You don't have to hear me talking about the need to codify 4(a)(1 1/2) which you've been hearing for three years-plus. So I'm sure this is very exciting to Sebastian and all of the people at the SEC as well.

MR. GRAHAM: Do you have a sense of the impact it's going to have on secondary market liquidity?

MS. TIERNEY: One thing that we thought would be really interesting -- and we're going to put this out in the next week or so -- was we did a review of all of the secondary liquidity programs that we'd done over the past two years, and we looked at the information that issuers provided to participants in our market to get a sense of where there might be friction points that might be uncomfortable.

What we found that was in about -- I think the number is 74 percent of the cases -- 74 percent of the transactions that we did, U.S. GAAP financials were provided. That was a good percentage. We were pretty happy with that. Some of the companies that we work with didn't have U.S. GAAP financials. They just provided financial statements. But 74 percent provided two years of GAAP financial statements.

Another requirement is that if the balance sheet is more than six months old, you have to provide interim financial statements. That we saw less of, I think 38 percent of the transactions that we did, included interims. And I think the market -- and Stephen, he probably knows better than I, but I just don't think the market put that much emphasis on interims, and companies didn't really consider them to be that material because they were growing so fast or they were expanding in different ways. So that's something that we felt was interesting.

So I think that what's going to happen is that to the extent a company is sponsoring a liquidity event, they're either allowing their shareholders to transfer securities to a buyer and they've got a good relationship with the seller or they've engaged a platform or some kind, NASDAQ, private market, whomever to actually facilitate the liquidity program. 4(a)(7) is going to become the exemption of choice because it clears out all the noise around the opinion practice and also the cost of the exercise. To the extent the issuer is not willing to provide information, 4(a)(7) also makes it very clear that it's a non-exclusive safe harbor. So 4(a)(1 1/2) construct still exists as currently applied. So now you have two options.

The only other exemption that we really see utilized our in our space is Rule 144. And in the private company space, that means you have to hold the stock for 12 months, and it doesn't include tacking period for holding options in most cases. So for most of the people that we work with, the shareholders that we work with, they can't satisfy 144. So, again, 4(a)(7) is an excellent choice for them and 4(a)(1 1/2) still operates to give them more choices.

MR. GRAHAM: Do you see from -- do you see the potential for friction in the -- kind of in the new 4(a)(7) rule related to the information requirement and the potential liability of issuers?

MS. TIERNEY: I've heard that question a bit. I would think that to the extent that an issuer is providing disclosure, it has -- in the context of the exemption, the information is to be provided to sellers and buyers. I don't think there's an increased level of information. If a company is providing fraudulent information, it has liability already under the securities laws. So I don't think there's a greater degree of liability. And again, it's the company's option if they want to provide the information.

MR. GRAHAM: Is there anything else that you think we need to do as a committee to bring additional clarification to anything?

MS. TIERNEY: There are some -- I think the part that's tricky is that the exemption's built into the statute, not into a rule. So the staff doesn't have the ability to actually make changes themselves I don't think. So we are actually working with some members of Congress on some technical amendments that we think would be helpful where there's terminology used that's not specific to the securities laws.

So it that goes forward, I'm sure I would come back to the committee and sort of let you know what we're doing and potentially get a recommendation, if you all agree, to support a technical amendment.

And one of the things that took us by surprise was the change of the information requirement to something that the purchaser can wave which was in an earlier version of the bill to the actual requirement that it be provided. So we think we're still working through that concept as well.

MR. GRAHAM: Okay. We were supposed to spend a moment or two on what's happening on the congressional side of things, and I skipped over that.

Sara.

MS. HANKS: Because it's less interesting, I think, than what Annemarie was talking about. One thing with respect to the 4(a)(7) changes, which I think were good as far as they go, it's not the answer to -- it's not the liquidity answer that we're looking for yet. There is other stuff that needs to be done. I mean one of the things that 4(a)(7) answers is the ability when you are doing a resale to an accredited investor, you can now not have to bother with state regulations, and that's nice. But we need that for all of the private market securities that are going to be traded, and that does not yet exist.

So I'm going to totally gallop through a few of the congressional initiatives that are out there just to make sure that everyone knows what's out there and who knows whether any of these will ever go anywhere in that we are now just a few days away from Super Tuesday. So who knows whether this will go anywhere.

There's been a lot of interest in Congress in making changes to the securities laws for fostering capital formation over the course of the last few years. The JOBS Act, of course, and all of the various initiatives that were gathered into the JOBS Act is one of the best examples of that, but this is a continuing process. And there's a few bills floating around congress at the moment that could eventually end up being JOBS Act 2.0, 3.0, whatever you want to call it this week.

On February 1st, the House passed with overwhelming bipartisan support a bill that would amend the definition of accredited investor in Section 2(a)(15) of the Securities Act, which relates to Section 4(a)(5) of the Securities Act, which is an exemption that I did not mention this morning because it doesn't get used. The staff would never be able to say this, but it's an identical definition for an unused exemption that is identical to the one that does get used in Regulation D.

I am assuming -- and the staff does not have to answer this, of course, that the staff would likely, as they have done in the past, change both definitions in tandem, because that would be the logical thing to do, and I don't think they have any prohibition on that.

What the definition would do is some of the things we've just been talking about: codify current net worth and income thresholds, include persons who the SEC determines by regulation to have demonstrable educational job experience to qualify such persons of having professional knowledge of a subject related to a particular investment such that they're allowed to be accredited investors. And the SEC, of course, can expand this.

There is another set of bills that would establish the Office of the Advocate for Small Business Capital Formation, which would, in effect, take -- probably take this committee and make it a statutory committee, appoint an advocate for the business sort of parallel to the current investor advocate, which is a separate office within the Commission and also require the Commission to respond formally to the recommendations made in the annual meeting every year that the -- I forget what it's called now, but the Small Business Forum is the short name.

Anyone watching who isn't aware of this, this happens usually the week before Thanksgiving every year, and it's a really entertaining and democratic process where a lot of people other than the usual talking heads can be heard by the Commission. So, everyone, that is webcast and that's -- all that the afternoon breakout sessions are usually broadcast by phone, and so people should participate wherever they are.

Also, February, the House passed a package of bills titled: The Capital Markets Improvement Act of

2015. It's got a number of different elements, including changes to Rule 701, which is an exemption for securities issued to compensatory benefit plans, E swaps, which would increase the level at which a written plan has to be disclosed. There's -- it would also include the M&A broker exemption that we talked about earlier, the exemption that the SEC has issued by no action letter to certain people acting as M&A brokers or business finders put that into law. It's fine as far as it goes, but it's already in the no action.

It would -- the collection of bills would also exempt emerging market -- emerging growth companies from having to use XBRL, which is the tagging system whereby you say this is our net revenues, and it's always -- so that somebody who searched doing machine searching of filings could compare apples to apples in a company's accounts. It's a useful idea, but it is very difficult to do in some circumstances. So that burden would be reduced, and there's also a proposal that the SEC be directed to draft a rule providing a safe harbor for covered investment fund research reports.

Whether any of these are going to go anywhere is debatable. A veto threat is a possibility with respect to that last collection that I mentioned. And as I said, we're a few days away from Super Tuesday, so who knows.

MR. GRAHAM: Nice wrap-up. Thank you.

Well, again, one of the questions that we have to keep asking ourselves is: What is in the way of efficient capital formation for small business? As I mentioned earlier, in terms of useful rulemaking and policy, I think that three things that seem most important to me, and that's liquidity, complexity and certainty.

I think in terms of liquidity, no one is going to get into something if they can't get out of it. In terms of complexity, rules that should take you to a good place are -- it's a nice idea. But if they're so complex that they -- as to be not useful, then of course they become not useful. Certainty is the other one. It's -- make sure that the whatever rules that we have out there, there's some degree of certainty associated with it.

I think that's one reason why -- I mean I don't know, but I think that's probably one reason 506(c) is slow on the uptake because of all of the uncertainty that kind of surrounded verification. I guess that seems to be settling down a bit, but we'll see what the future holds. But I think we've talked about a few things today that probably are worth following up on. The definition of accredited investor, no need to say anything more at this time, but I reiterate that everyone should get a copy of the report and read it and let's start exchanging ideas.

The -- we talked about, again, the issue with finders versus brokers. That's -- I think many of us think that that's important, and I think many of us think that small steps could be taken that could have a noticeable impact.

The whole issue with respect to one-size-fits-all in the markets, that's one that I think continues to be significant. I think people understand that fact, but there's still I think work to be done in order to find a way to structure markets so they're more conducive or more friendly to smaller public companies.

And then of course we talked about outreach. I think that's something that we haven't focused on, I think sufficiently. And again, whenever -- when you think of outreach, you tend to think in terms of trying to educate the companies, trying to educate the issuers. But I think this may include also educating capital sources and maybe thinking in terms of partnering with industry groups.

There's much work to be done, and as in most cases, we have to be careful not to let perfection be kind of the enemy of the very good. And so I think that hopefully we can begin to take some incremental steps that will have a real impact. And with that, I wanted to give everybody an opportunity to give some of their ideas before I wrap things up.

So, Catherine.

MS. MOTT: Thank you, Stephen. Stephen and Sara, could we possibly review the definition of general solicitation? Here's my thoughts about that is that -- and I think that's why you see more 506(b) offerings than you do (c). If we could, carve out demo days or what we call demo days, venture fair, pitch competitions as not general solicitation.

I think that a lot of attorneys are saying to their clients, look, when you go to these demo days, don't talk about raising money; just talk about what your company does because you're going to cross that threshold that means you have to file 506(c), and you can't go back and file for 506(b) once you go down that path.

And so what that then does is then the whole venture community says, well, forget it, I don't want -- look at this company now. So I think we have some -- we could simplify that definition so that we understand it so that the issuers understand how they play in the marketplace.

MR. GRAHAM: Thank you.

Sebastian, I can't call up those CDIs. Is --

MR. GOMEZ: Catherine and Steve, I think that's a good topic to touch upon. There is no black and white definition of what general solicitation is. The staff has been getting a lot of questions or had been getting a lot of questions as to what constitutes or doesn't constitute. The staff provided some guidance in the form of CDIs.

There was also no action letter that the staff issued last year providing some insight on that. But I think if the committee desires to do so, that might be an interesting topic where we could get someone from the staff to present to the committee as to what the staff has done with respect to interpretive guidance and no action letters.

MR. GRAHAM: So this might be another situation where we're moving the ball forward, but maybe we're at the 50-yard line in terms of having sufficient certainty?

MR. GOMEZ: I just -- I'm not sure where the --

MR. GRAHAM: 30-yard line?

MR. GOMEZ: -- goal line is. And I think if you ask different people --

MR. GRAHAM: 15-yard line?

MR. GOMEZ: -- where the goal line is, I think people would have different ideas. And in part it's because general solicitation is not black and white, and it's facts and circumstances. So in many ways what the staff was trying to do was provide some guidance as to the things that may be and may not be general solicitation.

It used to be that about 20 years ago there was quite a lot of no action guidance in this area, and then in many ways what the staff did is go back and look at that no action guidance in the form of CDIs. And the new letter that the staff provided in essence update, bring forward that guidance.

In some respects it did not change from what was before, and in some other respects there was what some may view as potential expansion as to what had been done before. So it might be a topic that is worth for the committee to hear from the staff and then the committee can always decide whether we are on the 50-yard line or whether we are almost at the touchdown.

MR. GRAHAM: All right.

MR. YADLEY: I think that's a great idea. I was yesterday talking with a British friend. An American was saying he thought he liked cricket, but he was always confused because he never knew when the game ended, and there actually are rules for when the game ends.

So I think where the goal line is is very important, and so I think the Commission and the staff should be commended for bringing out the lore and the prior guidance which was there and expanding it to the extent you can, and I think our committee may have views about in the same way that Rule 147 has changed with technology and practice and communications that the goal line may in fact have moved in a way that we can promote capital formation and still protect investors and stay true to the language of the statute.

MR. GRAHAM: Annemarie, were you going to --

MS. TIERNEY: If we're going to stay on the general solicitation -- and that could be a little, kind of drilled down, I think one of the things that's in the current non-exclusive safe harbor for verification which is a real kind of friction point is that if you're verifying somebody under net worth, they -- it's only good for 90 days. And the documents have to be within a certain number of days.

Under self-certification under -- for 506(b) purposes, people certify one time a year that they're accredited. So I don't understand why for 506(c) purposes now you're putting people in a bucket where they have to potentially be certified at least once a quarter. And I know for angels that we were dealing with, it was really painful for them. Like we just did this. And if it was just past the 90-day and 92nd day from the date that we did it, maybe we verified on March 1st, but the deal didn't close until two months after that, and then we had -- it was very painful.

I don't understand the investor protection or other policy position that's supported by that policy. But to the extent you can get unnecessary friction out of the verification process, I think that would go a long way to helping people think it was worth going through the process.

MR. GRAHAM: Thanks.

Jonathan.

MR. NELSON: I would love to know what sort of things can we do as a committee. Can we resolve to recommend something that general solicitation be defined as X, Y and Z? Can we --

MS. HANKS: We can try.

MR. NELSON: This is not the opinion of the SEC or the President, but as the people who have been asked to give our opinions, how do we give our opinions? Is it a discussion? Is it a dialogue? What's the end product that we're delivering?

MR. GRAHAM: What's kind of the mechanism? One thing that I would commend you to are the recommendations as the committee in past years. And what -- they're all on the website I'm sure. What we do is we have meetings like this. And the issues come up, and there's some issues that we decide then to kind of focus on and drill down on. And with those issues as we move toward consensus, we develop recommendations, and then we consider recommendations specifically and talk about them, amend them, pass them.

MR. GUTIERREZ: I'd like to make a comment in closing. When I think about the issue of capital formation, I always think of the two players, right? There's the business and then there's the capital provider. What I'd like to see from this committee is obviously the issues that we've discussed that are in the way of businesses being able to access capital, whether that's education, whether that's not knowing exactly what the options are that our out there, whether that's maneuvering through this maze of regulatory environment in terms of issuing. So there's that whole, I guess, effort.

I'd also like to raise the issue of part of the inefficiency in the capital markets has to be who the providers are. So one of the conversations we haven't talked about are how do we help foster capital sources that may have better understanding and knowledge base of these businesses, whether that's because we diversify who those capital sources are, I mean specifically talking about women and minority-led investment firms and whether or not this committee can be engaged in that or just through different types of folks from different industries that may or may not believe or understand that they could be part of the capital source universe.

So I'm not sure if that's an endeavor that this committee could take on, but clearly that is part of this discussion of making capital formation more efficient is taking a look at the face of the capital providers.

MR. GRAHAM: For me that's included under outreach. I mean you've got people with pools of money that want something. And they know what they want, and they're willing to pay for it. And then you have businesses that -- saying, gee, I can do this or this or this. And -- but there's only one thing that this capital source wants. And if -- it's that kind of disconnect that's out there that we should be able to help -- kind of help, kind of get things aligned in the right way.

MS. YAMANAKA: I'd like to chime in on that. I really support that idea. I think that there's a lot of tension that have applied to traditional sources, and the world has changed out there. We're competing internationally more. They have different types of market sources for capital formation within their own countries and entities, and I think we're at a competitive disadvantage if we don't at least offer something similar, and it could be through minorities, women-owned businesses.

But what's good in the opportunities for that group is going to be good for small business in general. So I think that this is a perfect opportunity to expand our opportunities and how we look at things. I do think we need to fix and make -- address how things are done traditionally. But to really try to throw -- and I don't mean to create a whole bunch of work for everybody. I really apologize.

But I think it's already happening underneath. It's percolating under the radar. People don't know they're doing certain things. In some ways perhaps they're a little bit not in compliance. But if we can take a look, understand what is currently happening, magnify the positive impacts of that, start to measure how much of that capital formation actually is occurring that we can't track because I think John was saying earlier we don't -- they don't know because they don't file, right? That it might be very, very interesting to find out where that is leading to in the chain upwards.

MR. GRAHAM: Okay. Anyone else?

MR. HAHN: I've got -- a potential topic for discussion is around short-selling disclosures. So in December, NASDAQ filed a rulemaking petition with the SEC asking it to take action to require disclosures of investors' short positions in parity with existing disclosure requirements for long positions.

So currently investment managers in funds must publicly disclose long positions and significant long transactions on a quarterly basis. Short positions, on the other hand, are only reported in an aggregate manner by the national exchanges. Lack of transparency creates an environment with potential for manipulative or abusive conduct.

I'm not sure about other industries, but in biotech we're particularly vulnerable to short manipulation due to the thinly traded stock and long time between news events. Just to be clear, nobody's talking about -- nobody's proposing any limits on short selling. It's simply an issue of equitable transparency in reporting.

MR. GRAHAM: Okay. That's a good point.

Annemarie.

MS. TIERNEY: So as a result of the JOBS Act and other SEC initiatives, we have a much wider range of options now for capital raise we've already discussed today. I think the committee should take a look at places where -- you said earlier that there's complications in what's out there that potentially makes these exemptions not interesting to companies. And we touched on earlier the idea that you could be a tier two, Reg A company putting out periodic information, and there's no resale safe harbor available to you under the federal securities laws.

So one of the things I think we probably might be worth looking into for us is supporting some kind of amendment to Section 18 to cover transactions that occur -- securities issued under tier two to the extent that the companies voluntarily periodically reporting. I've got all my words right. But that just seems odd to me. They're periodically reporting, they're putting information in the market. But you don't have a resale exemption for your shareholders.

MR. GRAHAM: Right.

MS. HANKS: I think that's an important thing. I think there's a lot of people who don't understand that that is actually a problem out there.

MS. TIERNEY: You told me, Sara. So I believe it.

MR. GRAHAM: So, Lisa.

MS. SHIMKAT: I kind of want to just know --

we've talked about a lot of things, but -- so what are the next action steps? Especially -- obviously I am more heavily or could potentially be more heavily involved in the outreach side and the education. In seeing the report that we had earlier, there was a lot of good points there and a lot of discussion around the information and the statistics that maybe sometimes statistics open our eyes to not really our shortcomings, but maybe we're focusing on the wrong issue.

And so as we looked at getting additional training out there for the decision makers, who are people going to, where are they getting their information, and it's just like trying to go to the newspaper to try to advertise to millennials. Are we doing what we need to do to get information out there when it comes to the different types of equity?

So what would the next steps be? I mean what --

MR. GRAHAM: What we do is following this meeting, Sara and I and the staff will try to make some sense of our discussions, and then we will kind of formulate a path forward and you all will be able to react to that.

Patrick, did you have anything else you want to add?

MR. REARDON: I would say studying sources of liquidity because I know the investors I have represented are always interested in small company exit strategies, that they're interested in that. So that would be a topic that I would be interested in.

MR. NELSON: I'd be interested in talking to some of the crowdfunding platforms in Europe, like Cedars, and some of maybe the regulators in the EU and just hear from them about how has it gone to not have an accredited investor limit, have they noticed fraud, that sort of stuff. It would be interesting to, I don't know, talk with someone like Kiva who does capital formation overseas in a very interesting way. Would that be considered a securities offering if a group of people got together online and -- like to an entrepreneur here? I don't know. That sort of stuff would be fascinating to me.

MR. GRAHAM: I don't think we've ever brought anybody from overseas. I don't know if that's in our budget.

MR. GOMEZ: I thought your law firm's budget was -- and, Steve, we can follow up on that and see what the options are.

MR. GRAHAM: Okay. So, Catherine, anything else? Okay. Kyle?

MR. HAUPTMAN: Just to that, whether we have a live human being here from Europe or not, their perspective I think is important. Somebody just told me the other day that they wanted to list their company on the French exchange for startups. They had to go abroad to meet their needs. It's just a sentence I'd like to never hear again.

MR. GRAHAM: Brian? Xavier? Robert?

All right. Then can I entertain a motion to adjourn four minutes early?

MR. YADLEY: Just before we do that, just one more thing. We're talking about budget. Obviously, our budget is only for four meetings a year. And we talked informally earlier about limitations on dates for meetings and the importance of having a facility that will accommodate our requirements under the Advisory Committee Act be public and so on. But our committee only has 13 members.

So as we try and finalize the dates for this year, if two or three people can't be there, that's a real chunk of the committee. And so to the extent we can finalize the dates for May and October and circulate them before they're finalized so that you see how many committee members would be not just inconvenienced by, for example, I have a public company client annual meeting and board meeting that has been moved twice, and it's --

MR. GRAHAM: I agree with you 100 percent, and we will get right on that and see if we can't get those things pinned down. But we need to respect everyone's schedule and respect my promise to get your out of here at 3:30.

PARTICIPANT: Do you need a second?

MR. GRAHAM: Do I need a second? Yes. Okay. All those in favor?

(Chorus of ayes.)

MR. GRAHAM: And --

(Whereupon, at 3:30 p.m., the committee meeting was concluded.)

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PROOFREADER'S CERTIFICATE

In The Matter of: ADVISORY COMMITTE ON SMALL AND EMERGING COMPANIES

File Number: OS-0225

Date: February 25, 2016

Location: Washington, D.C.

This is to certify that I, Nicholas Wagner, (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.

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