U.S. SECURITIES AND EXCHANGE COMMISSION

SMALL BUSINESS CAPITAL FORMATION

ADVISORY COMMITTEE MEETING

Friday, January 29, 2021

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Via WebEx Teleconference

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

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PROCEEDINGS

INTRODUCTION

MS. GARRETT: Good morning. I hereby call the January 29, 2021 meeting of the SEC Small Business Capital Formation Advisory Committee to order.

It is nice to see everyone again in this new year. I also welcome the members of the public who have tuned in to watch the meeting via webcast on SEC.gov.

Julie, do we have a quorum for the meeting?

MS. DAVIS: We do have a quorum and I will, at this time, give our lovely mandatory SEC staff disclaimer which is that any views that members of the SEC staff express today are our own and do not necessarily reflect the views of the Commission, any of the commissioners or any of our colleagues on the staff. Additionally, any SEC commissioners or staff who appear on videos from their offices will appear only without a mask if they are working alone with the door shut in accordance with guidance following the recent executive order. Thank you.

MS. GARRETT: Thank you, Julie. I – first of all, for the committee, I wanted to let people know that I am pleased to welcome back to the committee, Mike Pieciak. He is the commissioner of the Vermont Department of Financial Regulation, and Mike will

replace Melanie Lubin as NASAA's representative on the committee. We appreciate Melanie's service on the committee and we are pleased to welcome back Mike. Mike will be joining the meeting later this morning.

In 2020 our committee has spent a lot of time discussing how COVID-19 severely impacted small businesses. Unfortunately, small businesses are still struggling and closing as a result of the pandemic. Although COVID-19 and its effect on small businesses will not specifically be on our agenda today, the committee is mindful of the hardships facing small businesses on a day-to-day basis and I'm sure that we will be discussing these issues in future meetings.

Over the past year the committee has spent a good portion of our time focused on the ways that the companies access capital through the private markets. This morning we will focus on the public company portion of the committee's statutory mandate which covers public companies with a public float up to $250 million.

We have invited speakers from the long-term stock exchange, OTC markets, NASDAQ, and the New York Stock Exchange to share some of the trends and dynamics that they are observing as they engage with smaller public companies and later-stage private companies considering going public. These trading venues bring a

wealth of insight into the issues smaller public companies face and we look forward to a dialogue with the exchanges.

Today the committee is not aiming to make any specific recommendations on the policy item relating to smaller public companies, but to instead lay the groundwork for work to come and to shine a spotlight on the experiences of the smaller companies raising capital whose stories are often untold.

After lunch we will turn to a new SEC proposal that on a temporary basis would permit an issuer to provide equity compensation to certain gig economy workers. Compensating workers with equity is a topic on which a number of committee members have experienced, and I hope that we can provide valuable perspective to the Commission.

Before we start the meeting, I would like to share a few reminders for the virtual environment. Please unmute your microphone when you speak and then go back on mute when you are finished. If you'd like to be recognized to speak, please use the chat function in WebEx. And when you do speak, please first state your name so that everyone, including the court reporter and members of the public, know who is speaking.

This morning we are pleased to have with us

Commissioner Peirce, Commissioner Roisman, and Commissioner Crenshaw. Unfortunately, the newly designated acting chair of the SEC, Allison Lee, had a conflict and is not able to join us today. We welcome the commissioners to the meeting, and we look forward to your opening remarks.

Commissioner Peirce?

COMMISSIONER PEIRCE: Thank you, Carla and thanks to members of the committee for putting together and agenda that touches on a variety of important subjects. It's encouraging to see you all back to work in 2021. I hope that at some point later this year we'll be able to meet in person. Of course, that's going to depend on vaccination efforts against the pandemic, which continues to have devastating effects, including on small businesses across America.

The recently published annual report from our Office of the Advocate for Small Business Capital Formation provides a sobering snapshot of the harmful effects of COVID-19 in the first three quarters of 2020. A 27 percent decrease in the number of small businesses, drastic reductions in revenue of up to 70 percent in certain industries over the same period, and a reduction in headcount for nearly half of all small businesses.

Facilitating access to capital for small business must remain a priority for the Commission in the coming months and this committee can play an important role in identifying pragmatic solutions and spotlighting specific issues for specific communities. I look forward to your continued engagement on these issues.

I also look forward to today's other agenda items. When considering whether to go public, companies have to weigh the cost they anticipate facing as public companies against the benefits of being public. Among the anticipated costs are the costs associated with making required disclosures which include disclosures of material information. To what extent do companies consider the potential for future disclosure requirements that are not tethered to a principal of materiality but instead reflect the interest of an ever-increasing group of so-called stakeholders.

One benefit companies hope for in going public is a liquid market for their stock, but this benefit remains out of reach for many small public companies. Are there any particular market structure changes that would facilitate better liquidity for companies with thinly traded securities?

A final question or two for this discussion

relates to smaller public companies' experience with transfer agents. What are the primary concerns that smaller companies have when working with a transfer agent that the Commission -- and what are the concerns about the Commission's existing rules and what can we do as we modernize our transfer agent rules to address small company concerns?

The last item on today's agenda is a discussion of the Commission's proposed rule to modernize the framework that allows employees and other workers to receive equity compensation from their company. This was a proposal that I was happy to support and I look forward to your feedback on the proper scope of these rules.

As proposed in the gig workers release, only platform workers that provide services would be eligible to receive equity compensation. Workers that sell goods through the company's marketplace platform wouldn't be eligible. Is there a reason to limit participation to one type of gig economy workers?

Along these lines too, my fellow commissioner's question, why gig workers should be singled out for a pilot program when other types of alternative work arrangements have existed for a long time. Should we expand the pilot to include additional

types of workers? The proposal also would limit a gig workers equity compensation to no more than 15 percent of the value of compensation received during a 12-month period and no more than $75,000 of such compensation received during a 36-month period. Are these caps unduly complex or even unnecessary?

Thanks to the committee and the panelists for taking time to be with us today and thank you to Martha Miller and her team for their hard work in publishing their annual report and all the other work that they have done throughout 2020 and I look forward to today's discussions. Thank you.

MS. GARRETT: Thank you, Commissioner Peirce.

Commissioner Roisman? Commissioner Roisman, I think you are on mute.

COMMISSIONER ROISMAN: I think I got it now. Thanks, Carla.

So thank you, Carla, and good morning, everyone. I'm very pleased to be here today to hear from all of you. It's almost a year in and it seems unnecessary to comment on the fact that the format of this event is not out typical format or on the fact that the Commission, this committee, and Martha and her team have been able to continue this important work in the face of unprecedented circumstances.

We, here at the SEC, have slipped relatively easily into remote work. And while there have been a few hiccups along the way, many of us have grown accustomed to this new normal. This ease and acclimation, however, are all the more reason to highlight the work of this committee. Not every enterprise in America can so easily acclimate. Not every business lends itself to remote work and not every business is equipped to run with a remote workforce.

As the 2020 Annual Report from Martha's office so cogently lays out, the last year has been crushing for many small businesses. While larger companies have relied on reserves to pull through or to retool or reorient for the pandemic world, smaller companies have floundered, and many have shut their doors. The toll has fallen heavily on women and minority-owned businesses. It'd disheartening to see our small businesses struggling and to see the rippling effects their hardships wreak on their workers and surrounding communities.

With vaccines rolling out throughout the country, we can hope that 2021 will bring better days for all of us and especially for entrepreneurs and small business owners and their workers. As these companies emerge from the COVID-19 experience, it's vital that capital will be waiting for them so that they can rebuild quickly and soundly. The committee and the OASB were created in recognition of the fact that the SEC's orientation has not always been toward the smaller company or the company that will never have a big IPO, but that nonetheless is profitable, stable and valuable to its customers, investors, and communities.

OASD -- AOSB has done remarkable work reaching out to many types of small businesses and entrepreneurs across the country, an effort that I believe has had enormous impact in the short span of the time the office has been up and running. Similarly, this committee's work, including your recent recommendations last spring regarding crowdfunding relief, have been vital to the Commission's understanding of small business needs. I'm truly grateful for all your work and urge that we need your voices now, more than ever, to advise the Commission on what steps we can take to help small businesses looking to rebuild.

We recently expanded 701 to provide access to profit sharing for more workers and, like Commissioner Peirce, I would also note my colleague's interest in perhaps expanding that. So my question is what else can we do to make smaller and younger companies better able to compete for talent?

We've seen the options for capital raising proliferate over the last several years, revitalizing Reg A, expanding the availability of private offerings, and introducing brand new concepts such as Regulation CF. What other innovations should we consider? What has been the most useful to smaller companies and what could be improved?

I've always appreciated the insights this group provides to the Commission and I want to thank you again for your continued engagement and guidance. I really look forward to your ideas you will develop over the coming year and want to stress that my virtual door, and real door one day, is open. Thank you again.

MS. GARRETT: Thank you, Commissioner Roisman.

Commissioner Crenshaw?

COMMISSIONER CRENSHAW: Good morning, everyone, and thank you, Carla, and all the members of the committee, for being here today. I am grateful for your time and for your willingness to think about how the Commission can support small businesses and entrepreneurs and their investors.

This is my first time attending a meeting of the SEC Small Business Capital Formation Advisory Committee. I will try to get that straight as commissioner and it's really great to be here. And

while some of you know already -- and while I know some of you already, I look forward to engaging with each of you. And as my fellow commissioners have mentioned, virtually for now, but hopefully one day in person. Hopefully, someday sooner rather than later.

I want to begin by extending my appreciation to the SEC's Office of the Advocate for Small Business Capital Formation. Despite the challenges of the last year, you all have put together a thorough and detailed report that really brings attention to a lot of significant issues and you've raised some critical questions for us to consider. I think it's fitting that the first matter on the agenda is a discussion of the OASB's annual report and its key findings.

One item, as you all know, addressed in the report and that I'm certain is top of mind for many of us, is the devastating impact that COVID has had on small business and of course, my fellow commissioners have mentioned this already. And I do hope you will be able to devote at least some time today to thinking about what additional steps the Commission might be able to take to help businesses get back up and running as we enter the next phase, hopefully next phase I'll say, of the pandemic.

A second troubling, but unfortunately not

surprising, finding in the report is the disparate impact the pandemic owned by women and minorities. And this is certainly not a new problem. The report details the larger backdrop of structural inequities and imbalances in our financial markets. Specifically, the annual report highlights the ways in which our financial system has consistently offered investors more opportunities to invest in businesses owned and advised by white males and fewer opportunities to invest in businesses owned and advised by women and minorities.

The report further illustrates the greater challenges women and minority-owned businesses face when seeking funding and investors. I think one of the silver linings of 2020 is that there is an increased national focus and recognition of the ways our economy fails to serve community of color. I do hope that the committee will use this opportunity to consider what concrete steps we could take to work toward addressing these barriers.

And some questions I would be interested in hearing your views on include how do we improve access to funding for historically underrepresented groups and how do we encourage broker dealers, fund managers, investment banks, to facilitate offerings for these groups using their networks. Could we increase diversity among portfolio managers? Would that make our markets more inclusive? Are there ways for the Commission to encourage institutional investors, public funds and large private institutional investors, to allocate investments to more businesses with women and minority founders? And what is needed to break the cycle of what the annual report describes as “pattern matching?” And of course, I welcome any thoughts you all have on the subject. There's no easy solution but I really think this is something that we need to work through together.

As has also been mentioned, I know you're considering this morning current trends among smaller reporting companies. And we all know the important role that smaller public companies play in our economy and the value they bring to our communities. In a good year, smaller public companies face a number of challenges, from the threat of corporate giants to the consequences of having less research coverage. OASB has done a good job of highlighting these challenges and the unique circumstances these companies faced in 2020.

I'm sure we will discuss many of them today, but there are a few I am particularly interested in hearing your views on. The first, obviously, is as we've heard a bunch today, is COVID. The lack of

economic activity resulting from this prolonged quarantine has closed a lot of smaller businesses. And while some have obtained federal aid, others have had a more difficult time navigating that process.

I think it would be helpful today if you could consider some of the following questions. What are the most pressing needs right now of these smaller companies? Are the existing COVID-relief measures effective? And what else can the agency do to help these companies get back on their feet.

The second 2020 trend I want to highlight is SPACS. Everyone is talking about the rise of SPACS and I'm certainly interested in hearing whether the dramatic increase in SPACS over the last year has impacted smaller companies and if so, how.

And finally, this afternoon when you consider the compensatory offering rule-making, I'd really be interested in hearing your thoughts on whether the Commission should be asking companies to use compensatory offerings as an additional benefit on top of cash compensation rather than as a replacement for a portion of their cash compensation. I'm also interested in hearing how these workers might withstand the liquidity risks of these offerings.

Thank you all so much. That was a little

longer than I intended but it was my first meeting. So I appreciate all your time and I really look forward to today's discussion.

MS. GARRETT: Thank you, Commissioner Crenshaw, and welcome your first committee meeting. We look forward to having you at future meetings. And thank you, Commissioners Peirce and Roisman, for all of your opening remarks.

And as the commissioners pointed out, the first item on the agenda is an overview of the SEC's Office of the Advocate for Small Business Capital Formation Fiscal Year 2020 Annual Report that was submitted to Congress on December 18, 2020.

I received the annual report yesterday in the mail and I will say that it is a very impressive document, and it is very thorough, and I was amazed by the information in it and also just the -- how pleasing and how well it looked. So thank you very much for putting that together and it's a great resource for everybody.

I'm happy to introduce Martha Miller, the Director of the Office of the Advocate for Small Business Capital Formation. Martha, we look forward to hearing from you about the annual report and the great work that your team has been doing.

OVERVIEW OF THE SEC'S OFFICE OF THE ADVOCATE FOR SMALL BUSINESS CAPITAL FORMATION FISCAL YEAR 2020 ANNUAL REPORT

MS. MILLER: Thank you very much, Carla. And I have to thank Hester, Elad, and Caroline, our commissioners, for the wonderful shout-outs. You are each wonderful hype women and men for the work that our team does, and I appreciate it.

And I want to also just start with a big thank you to our team. I know that you probably noticed last meeting I wasn't physically present or virtually present. I was actually with camera off watching the webcast like the rest of the public with a baby in my lap on parental leave. And me taking time away would not have been possible without the wonderful support of our team and willingness to work with me at all kinds of strange hours as I reengaged on this report.

To give you a little background on the report, which I know you've heard a couple of folks mention, we prepare this report not only because Congress asks us to do it but because it is core to our advocacy mission. And it provides us a platform to tell the story, not only of what our office has done but what is happening with capital raising using not only data but also anecdotes and communicated where there are opportunities to fix issues that small businesses and their investors face.

So I want to dive in and encourage you, to the extent that you have not got a physical copy of it or you haven't looked at this yet, to download a copy from our website. And if you have downloaded these slides from the advisory committee materials, you'll find a direct link to download that. There is more in the report than we could possibly cover in one meeting.

I want to give a quick preview of what our team will cover today as a brief overview. We'll give a couple of highlights from the year and then I'm going to turn the mike over for a discussion of capital raising trends and policy priorities followed by a brief Q & A from our committee members. If you look at the report in the beginning, you'll see that there is a lot. Our year was busy in spite of COVID and social distancing measures and we do a lot with engagement, as our commissioners indicated. It's core to how we operate.

I have often analogized our office to a megaphone, and I'll reiterate why I do that. Advocacy requires us to use our voice to speak for others and to do that, we need to get out of the DC bubble. Our report highlights some our engagements over the last year. You, our committee members, know how

intentionally we think about the issues impacting small business as well as the issues impacting women, minorities and other represented founders and their investors, and I welcome ideas that anyone who is watching, not just our committee members, has for how we can expand who we hear from.

You will also see a wonderful part of the report highlights the work of the advisory committee, who had a busy and productive year. There is a wonderful summary of the work of the committee and the recommendations, as well as responses from the Commission.

Another part of the report that you'll see is a highlight showing our team of advocates. You know many of these faces, for those who were a part of our in-person meetings, but I'll highlight that our team has grown with wonderful new talent to allow us to really fulfill our mission and mandate. They are the brains behind the office's operations and if you are looking at the PDF of this you can click and learn more about each of these talented members of our team and they're also on our website.

And I am excited now to hit the mute button and to change up who you are hearing from because you hear from me far too often, and to introduce Sebastian

Gomez, our wonderful deputy director, and Jenny Riegel, our policy manager, who are going to explore some highlights from the report. And while this report was absolutely a team effort that was touched by everyone, these two were instrumental in its production and they are owed significant gratitude and appreciation from me and the rest of the team for their leadership on it.

MR. GOMEZ: Well thank you, Martha. This is Sebastian Gomez and good morning, everyone. I'm delighted to be here.

So to jump directly into the data. At the core of our annual report is a wealth of data. The data we used in our report highlights and that we're highlighting today, supplement data that was provided by the SEC with the information from other sources that paint a more complete picture of capital raising --. By highlighting not just SEC data but other academics and thought leaders, we can paint a more complete picture of how capital is raised and deployed by investors so that we can more effectively target policy solutions.

So let's jump right into the capital raising trends. Our office is thinking about capital raising trends on both a macro and micro level. Looking at where capital is being raised and by whom across all different sectors. We think about geographic and

regional differences. We think about the impacts within different industries, demographics, and the stage of life cycle, spotlighting the initial impacts of COVID-19 through all of the sectors.

We're also going to highlight -- well, what we're going to do today is highlight only a small fraction of what's in the report. So as Martha encouraged, everyone, please take a look at the report, download a copy and take a look at it at your own time.

As you advisory committee members know, the fact is that there are multiple pathways to raising capital and the regulatory requirements often influence how much and how often those pathways are used. The bubbles you are seeing here in this slide are scaled to the amount of capital raised with private offerings in blue, from public offerings in orange. You will notice that there are three front runners, registered offerings, group 506(b), private placements under Regulation D, and the traditional private placements under Section 4(a)(2). Other new offering types are much smaller in comparison given both caps and proceeds, familiarity with the market, and other requirements for offerings.

Another important aspect of capital raising is the geographic differences across the country. In our report we include maps to illustrate areas of the country that are finding success as well as areas that are facing challenges. The darker colors you're going to see in the next slide indicate more capital raised in the state. I'm going to quickly click through some of the maps in our report, including the one you are seeing here with respect to Regulation D, equity crowdfunding, Regulation A, and registered offerings.

Jenny?

MS RIEGEL: Thank you. So I'm -- as Martha mentioned, I'm Jenny Riegel and I'm going to turn to some of the demographic data.

As you know, our office is -- with the unique challenges and variables affecting diverse -- whether across gender, racial, or geographic lines. It's important that we understand and actively seek out solutions to make sure the capital raising tools work for everyone.

To start, it's important to look at who owns small businesses across the country by ethnicity and race and as you can see, there is broad diversity among new entrepreneurs. However, as you'll see from the data that follows, that the portions of capital raised do not mirror business ownership or population figures at large.

This slide shows the percentage of employer firms owned by minorities across the country. Again, we're always looking to understand regional differences as we work to formulate policy recommendations. Bank capital doesn't work for every business and minority-owned businesses face greater challenges accessing bank capital. Our report breaks down this data further by race and ethnicity.

Minority founders are not as likely to receive venture capital funding as their white counterparts. It's particularly challenging for African American, Hispanic, and Middle Eastern founders who receive just 1, 2, and 3 percent, respectively, of the venture capital funding, despite that fact -- I'm sorry, despite the fact that ethnically diverse leadership teams have higher realized returns than companies with all-white leadership teams. This is data we explore in our report.

When diverse teams do raise capital, we see that they tend to raise more than all-white teams across successive rounds of funding. This is a bright spot and one that we'll circle back to later in our discussion today.

Just as we look at data on minority business ownership, we also focus on women-owned businesses and

their investors and their unique challenges in raising capital. Here we see a breakdown of women business ownership by demographic groups. Women founders received only 12 percent of venture capital dollars in 2019. This was consistent with 2017 levels but down from 2018 high water mark of 17 percent that we reported last year. Note that only three percent went to women-only founding teams.

Unlike the trend where ethnically and racially diverse teams tend to raise more per round, women-led teams tend to raise less than all-male founding teams. The median VC pre-money valuation is lower for both all women and mixed-gender teams. Additionally, women-founding teams tended to raise less per funding round in 2019 than their male-founding team counterparts

MS. MILLER: Jenny, thank you for this. Before we dive into some further data, I do want to pause in light of some of the wonderful comments that we had from the commissioners and just note we'll be looking more at some of the steps we recommend on this.

But I want to just emphasize and highlight here that we have a mismatch in who is founding companies, who is raising capital, and how much and on what terms they're able to raise. And if you just look at the data on this slide, when women are raising both

less capital per round and raising at lower valuations, together that means that women founders are giving up more equity than their male counterparts who often retain control of their companies through multiple rounds of funding.

So just looking at dollar amounts doesn't tell the whole story if we're not also looking -- dollar amounts of funding raised doesn't tell the complete story. And this puts women founders at a power imbalance that differs from male founders, a topic that you have probably seen in the news lately and one that we are closely attuned to. So back to talking through the data but I did want to just share that observation.

MR. GOMEZ: Thank you, Martha.

And I wanted to jump into the impacts of COVID-19 on capital raising. The committee has worked diligently to address some of these challenges that COVID-19 has brought on small businesses. We devoted a significant portion of our annual report, as the commissioners mentioned, to highlighting some of the initial impacts of COVID-19 that had been broadly felt across the country.

While small businesses had endured times of economic distress in the past and many noteworthy companies were born during downturns, the devastating

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impact of the virus and the uncertain duration are unlike any economic shock to date. Commissioner Peirce mentioned the 27 percent figure that we're highlighting in this slide. For every state where we have data, the number of small businesses have declined. Some states are seeing decreases of up to 40 percent, 30 percent, which can be attributed to a variety of reasons from changes in customer spending to social distancing measures to lower capital reserves.

As we look at the impact of COVID-19 on revenues we see a particularly harsh impact on businesses that require in-person interaction. Think of hospitality, retail, entertainment, transportation, personal services, food services, they all have seen a particularly harsh impact on their revenues.

This is a slide that you previously saw in our August 2020 meeting so I'm not going spend too much time discussing it today. As you are aware, founders and historically underrepresented groups have been disproportionately impacted, including minority and women founders. In the first few months of the pandemic, we saw small business closures disproportionately impacting women and minority-owned businesses.

Examining this COVID-19 impact on

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underrepresented groups is critical to remediating long-term gender and racial inequities in capital formation. There's more to come on this as we delve into our policies, priorities and proposed solutions.

Jenny?

MS. RIEGEL: As this committee is well aware, when Congress created our office, they specifically charged us with advocating for solutions to the challenges faced by small businesses and their investors from start up to small cap. Now that we've given an overview of some of the data from our report, we want to dive in on four key issues that we flag as priority areas for the Commission and Congress along with data underscoring why those issues matter as well as our proposed solution.

Sebastian?

MR. GOMEZ: So thank you, Jenny.

I'm going to take the first of our policies and priorities in our report and then addressing the challenges of offering complexity and frictions. This is a topic that you all are familiar with as advisory committee meetings -- committee members. But before we delve into offering complexity, I think it's important to -- and critical to underscore why well-functioning pipelines to capital are so important.

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Small businesses have an outside impact on job creation. The importance of small businesses come down to people and their livelihoods. Importantly, new small businesses have a significant impact on job creation and many of them need capital to build, grow and create jobs. But sources of --

(Audio temporarily drops.)

-- categories, money that the business makes, personal money that founders put into their business, and money from outside sources.

As this slide illustrates, looking at access to investor capital in a vacuum doesn't tell the whole story about how early-stage businesses find the capital they need. Personal funds and retained business earnings, while widely used across small businesses, are options that are generally available only to established companies or high net worth individuals. External capital is essential for many small businesses.

So thinking of external funding sources, bank financing might not be a viable option. This is something that Jenny alluded to earlier by noting the challenges that some face to access bank financing. During the initial startup stage they typically have minimal or no collateral and lack sufficient earning histories, tax returns, and performance track records

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for bank underwriting. And on top of that, many companies whose greatest asset is an intangible, like intellectual property, will be faced with banks looking at the entrepreneurs personally in order to see if they will be able to access capital.

So when entrepreneurs turn to our capital markets for financing, this is what they see. They need a complex set of rules. This is a summary of a chart that we prepare to reflect the 2020 changes to the rules from the capital formation adopting release and it underscores that point. The rule comes with decades of history that interweave congressional action, Commission rulemaking and caselaw, just to name a few of them, and they provide businesses and investors with different options to meet their capital and investment needs.

So how can we address this complexity when in the expanse offering structure? Significant changes have been made to the offering framework to reduce friction and complexity, but education of resources can help small businesses and their investors identify which options best fit their capital needs, their risk tolerance, and the long-term objectives, and how this will aid in compliance with the federal securities laws.

Educational resources also equip investors with appropriate tools to understand what information and other rights they have under the different types of offerings. As we think about targeted educational programs, we think of resources that are targeted to underrepresented groups that face challenges in raising capital to make equity more equitable.

MS. MILLER: Absolutely. And Sebastian, I think we talk about this a lot. A J.D. should not be a prerequisite to navigating capital raising.

MR. GOMEZ: Indeed, very true.

MS. RIEGEL: Thank you. So I'm going to cover the second policy and priority which is -- from our report which is bridging networks between founders and investors.

It is critical for companies to connect to investors with the right risk tolerance, industry experience and investing objectives for their company. As you can see from the numbers, angel investors have a significant impact on small businesses. Connecting with early-stage investors can positively impact a company's trajectory through mentorship, business relationships, and support with follow-on funding. Importantly, the mentoring and networking that angel investors provide can be even more influential in ecosystems outside traditional venture capital --

However, the right investors for a company may

lie outside a founder's personal network. These network challenges are exacerbated among underrepresented founders whose networks are statistically lower net worth. Investors tend to back companies close to home, with geographic distance increasing with later round raise. Part of the reason for this is that most early-stage investors take an active role with their portfolio companies and proximity makes it easier to monitor and stay engaged with the company. The benefits of proximity -- continued concentrations of capital in a few areas of the country, Silicon Valley, Boston, and New York -- the New York City area.

The fact that rural businesses face challenges raising capital is not surprising given that rural communities tend to have greater distances between founders and investors. The data in this graphic demonstrates the magnitude of these challenges. Rural areas account for 18 percent of the population and 17 percent of the smaller companies across the country. I mean look at the amount of capital raised across rural communities relative to their population. We see that rural businesses are raising far less.

Layered on top of the physical proximity challenges, pattern matching further reinforces artificial boundaries between investors and

entrepreneurs. This pattern matching then perpetuates a cycle that concentrates capital in limited geographies, ethnicities, genders, and educational backgrounds.

So how can we help bridge networks between founders and investors? We hear that both small businesses and their investors would benefit from additional certainty in a regulation of finders, as registered broker dealers tend to not support smaller, less complex, capital-raising transactions. We encourage the Commission to finalize a framework that delineates the legal obligations of persons who match small businesses with investors. Certainty for market participants will encourage compliance with the securities laws and provide clarity to investors on the protections in place when engaging a finder.

Sebastian?

MR. GOMEZ: Thank you, Jenny. Yeah, thank you.

Let's jump to the start of our policy priorities, diversifying access to capital from funds and sophisticated investors. Last year this committee highlighted some of the challenges, specifically with respect to regional funds and early-stage investment and retail access to investment and small businesses to full investment vehicles.

If you look at the aggregate statistics on small business fundraising it would imply that small businesses are receiving bigger checks and raising more capital. For example, if you look at the right-hand side of this slide and you look at Series C and -- funds are reinvesting in their existing portfolio as you can see demonstrated by the fact that the deal count has decreased in the third quarter of 2020 and they're deploying committed capital at record rates.

The report includes other data showing how other late-stage companies or their businesses are thriving but the sources of capital from two important sources are faring much more poorly. Emerging fund managers as well as smaller fund managers continue to decline in numbers. Both are important sources of capital for earlier-stage companies, companies with minority and women ownership and companies outside -- where most of the mega and private funds are based.

The above chart shows how fewer and fewer first-time funds are being raised, which farther concentrates investment decision-making in a smaller number of pockets without new market entrance. In a percentage of raises by small funds with less than $50 million in assets under management was on track to dip 40 percent for the first time in 2008, a 12-year low.

When we look at women and minorities, they still lag in representation among angel investors. This matters because of what Jenny talked about earlier, pattern matching. Pattern matching tell us that the founders are more likely to be funded by an investor of the same demographic background rather than a different one. In the patterns that we see across decisionmakers in venture capital firms will repeat in experience, results, in future investment dollars, has ripple effects across the industry. The problem not only exists within the decisionmakers at funds who are deploying capital to early-stage companies, the slide here shows that only 12 percent of them are women, but it also persists among limited partners who back this fund where 44 percent of them do not have a single woman decisionmaker.

So how can we address the unmet need among entrepreneurs seeking seed and early-stage capital, especially underrepresented founders? We encourage Congress and the Commission to explore initiatives to increase diversity among investment decisionmakers to help shift away from historic trends that negatively impact underrepresented founders.

We also encourage exploring ways to promote the formation of smaller regional funds to facilitate

growth of sustainable regional ecosystem through local vesting.

MS. MILLER: Thank you, Sebastian.

And I just -- I want to underscore a little bit of why this matters and to just highlight how critical this is for us. If you look at who is getting the earliest stages of capital, that is who goes on and is able to successfully raise the next round of capital. And that person who then raises the next round of capital is who goes on to create a public company and to have diversity of leadership that we see across the board.

So the ripple effects of what starts with the first dollars that come into a company impact who we see later on. The issues that we look at addressing in one area of the market have absolute ripple effects everywhere else and it starts with who is funding and how much capital is available for companies earlier in their stages.

So I could not underscore the importance of this topic enough and I'm happy to have further conversations with anyone interested on it, but let's dive in to that fourth policy priority.

MS. RIEGEL: Thank you, Martha. And yes, that is a very important point to underscore --

The fourth policy priority and our last one today, I know we're getting short on time, is the attractiveness of our public markets, which I know is a topic our speakers here today will care deeply about.

Turning to the data, in assessing trends among public companies it is important to look at both the number of public companies and their market cap. Since 1996 more than 90 percent of the stocks that had disappeared are those of small and micro-cap companies. As with each of these topics, we have lots more data in our annual report, including on the movement of corporate assets as an alternative measure.

We often compare the private markets and the public markets. And the size of the U.S. public market is significantly larger and the market for private investment via bio-AUM and venture capital fund. In addition, the amount managed by U.S. domestic mutual funds far exceeds the assets under management and the dry powder for both private buyouts and venture capital funds.

While we continue to see a significant number of companies preferring acquisition, exit trends have begun shifting back towards IPO. Many of these trends, I'm sure, will be covered by our wonderful speakers here today and we certainly don't want to steal their thunder

talking about why these trends exist.

Third quarter 2020 had a significant increase in both the number and total proceeds raised in IPO. Looking at the first three quarters of 2019 versus the first three quarters of 2020, there has been a 51 percent increase in the number of IPOs as well as an 81 percent increase in the IPO proceeds. While a report came out before the end of the fourth quarter, those trends continued through year-end.

So how can we foster a public company environment? Congress and the Commission should consider -- sorry, should continue to consider market innovations that could have the effect of incenting more companies to go public and remain public and evaluate both sides of the regulatory coin. On one side, what more can we do to encourage private companies to go public and on the other side of the coin, evaluate what more can be done to make sure remaining a public company is incentivized?

MS. MILLER: Thank you, Jenny. And I want to add an important note here that we don't view companies as having a binary choice, and I say "we," our office, of private versus public. Companies don't start out public and our pathways to capital need to support founders from idea to IPO to index, no matter your geography, industry, or demographic group and we are critically concerned with that which could not make our conversation today more relevant.

I will let Sebastian wrap us up. And we've got our annual report, which I will plug, please do download a copy. If you thought that the data that we presented here was interesting, there are magnitudes more; we couldn't even cover half of it in this. And we'll open it up for some Q & A.

Sebastian or Jenny, did you have anything else you wanted to add before we do so?

MR. GOMEZ: I would be delighted to take questions if there's any questions.

MR. SOLOMON: Yeah, I actually do have a question, Sebastian and Martha. Just -- I think it would be helpful to know, maybe from this group, how do we amplify this message? You know I mean this, the slide show, is a stunning depiction of trends I think most of us have known, we've been talking about this for a while but you know, even going -- I mean and obviously we've talked a lot about this and it just -- so there's nothing in there that surprises me but just seeing it laid out this way and going through and listening to you, your team, you know, present, it's really -- it's remarkable.

So for those of us that spend a decent chunk of our time advocating for improvements around capital formation for small businesses, how do we amplify this? How do we, you know, get it out there with key influencers and policymakers in order to ensure that this remains a core focus for the agency and, you know, as a critical part of any solution to, you know, build back better, I guess for lack of a better word?

MS. MILLER: Absolutely, Jeff, and I appreciate you asking this question. So I'll give a shameless plug, which is making sure people actually see this data and if you know people that are interested in these topics, make sure that they have seen our report and that they have seen the tapestry of what is happening, and they know the story of what it looks like to raise capital.

I will also say we're working very hard on these issues. These don't -- these are not going to go away from our agenda. This is core to what we are doing and so we will continue working on that. We welcome collaboration from anyone that has ideas. These are big problems. A lot of these are systemic. A lot of them are rooted in a myriad of different sources and -- I say "sources," origins of where the problems began and so it's going to take multifaceted solutions to address

these challenges.

So welcome collaboration on it but I think is the first -- making sure people actually know what the numbers show is critical because a lot of people are just not familiar.

MS. GARRETT: Sara, did you have a question?

MS. HANKS: Yeah, I had a question for Sebastian about some of the demographic measures. First, and I'll throw two questions, one is in the Where is Capital Being Raised analysis, what is -- where is the where? I mean are you measuring by reference to the companies' headquarters, primary place of business?

And then the second sort of related demographic question is when we look at the Where is the Capital Being Raised, it's mostly in California, but most of the people are in California. Is there a way of slicing and dicing that so you can do dollars raised by reference to size of population? Because I mean it's the answer that there's not much money being raised in Montana, that there aren't that many people in Montana.

MR. GOMEZ: Great question, Sara. And then for the first part of your question you're alluding to those heatmaps. And I do encourage everyone to take a look at that report because at the footnote to each of those heatmaps, we have some massive footnotes, and I

know that massive footnotes are not something that gets anyone excited unless you're a lawyer, but the reality is that those footnotes are actually describing where the data is coming from. It's data that DERA is providing to us and then it's based on the information that the company is reporting on their Form Bs, Regulation 8 filings, the Reg A filings, and that we see from the public filing.

So I do encourage everyone to take a look at those footnotes because I think you're going to find a lot of clarity there. What I particularly like is that even though you tend to see concentrations in the two codes, as you page through between Reg A, crowdfunding, public offerings, you see that that concentration does vary slightly but it does vary from state to state.

And then, Sara, to your last point, I think it's extremely important to look at it not just as numbers in the aggregate but in relation to population. See, this is something that Jenny touched on in one of the slides. We do have a section about rural areas. In one of the points of that was to actually highlight how it's actually not proportionally the amount that is being raised to the population. So the slide that Jenny brought up noted that even though the population is at 18 percent, if you look at how much is being raised under some of these exemptions, you're in the single digits. So it's not something that is proportional to the number of people that are in those areas. Great questions.

MS. HANKS: Thank you.

MS. RIEGEL: One thing I wanted to add to that is to the extent you see something in our report, and you have questions, and you don't think it is explained in the methodology, we welcome feedback. We welcome how we can improve this year over year and how we can better be transparent about the data that we are including in our report, so we welcome feedback on it. So if you don't -- if you look at the long footnotes that I worked hard to try to explain, we could always do better, and we can always improve kind of how we're describing how we're looking at methodology because it's so important to make sure that people feel confident with that data.

MS. GARRETT: Thank you, Jenny.

And Kesha, did you have a question?

MS. CASH: Yeah, a question/comment. I want to, first of all, thank you all for this report. My team and I and the folks that I work with, we talk about these stats and facts a lot and so it's nice to have this all consolidated as a report as we also advocate for addressing these issues. So thank you for that.

And I'll say in terms of getting the word out, we have -- we host graduate school student fellows each year and we have three onboard currently and we've invited them to the February 4th convening to discuss this report in more detail. So I think as we all think about people in our network as well as a couple of our founders that are specifically focused on lending to small businesses, invite them in, you know, each one, tell one more and I think we can get the word out about the great work that you all are doing.

A question that I have in regards to the point that was made in the report about distance, which resonated well, and we know it. I'm based in California, I have a distributed team, so we sort of cover different areas of the states, but I hadn't thought about it in the way that the report framed that distance issue. In addition to looking at venture capital based on distance and angel investing based on distance, have you all looked at the ecosystems in certain areas, because that's also, you know, part of that, you know, if someone invests or not, is there a ready-made ecosystem of support for those founders, accelerators, et cetera?

MS. MILLER: Kesha, those are great questions and I appreciate the plug. For those who are listening

and wondering what is on February 4th, that is our Capital Call Event. If you go to our office's website, you will see it and it's also linked in the SEC upcoming events. So thank you for plugging that and making sure that folks are joining in it.

To answer your question on how are we looking at ecosystems, we are definitely taking a look at that because it is complex. What infrastructure exists in a community really impacts the success that companies have in whether or not they can look to those who are nearby. There's a lot of research and a lot of academic focus on what local resources enable success and how companies are able to build and grow without having to go outside of their community because we do know that most initial capital is raised very close to home.

We showed the slides showing the 37-mile radius that's pretty average for those initial dollars coming in and a lot of that is because the early-stage investors take such an active role in the companies. As we look at ecosystems, we look at everything from interesting data on whether or not opening up a new direct flight line to a community from traditional hubs has an impact and the short answer is yes, that does. There's a lot to unpack there. We could do an entire day looking at kind of the web of resources from

accelerators to angel groups to later-state capital, but it is critical and we are always looking at it and we welcome feedback and perspective on it. So I appreciate you raising that, Kesha.

MS. GARRETT: Thank you. Does anybody else have any questions before we move on to the next topic on our agenda today?

MR. YADLEY: This Greg Yadley and I'd like to add my thanks to the staff at the office and congratulations, Martha, on your new child and it's great to see everyone.

Definitely success breeds success and successful sophisticated investors talk to each other just like everyone talks to each other and way down here in Florida we're envious of the Silicon Valley deals with three slides in a slide deck and an hour and $500,000 is raised and you go sequentially from there.

That also informs the fact that different kinds of offering attract different investors. So those Silicon Valley folks that write checks to each other's newfound companies, those aren't the people that are investing the crowdfunding offerings, to take an extreme example. So one of the efforts that we've talked about and I was glad to see on your priority list was pooled funds.

I am pleased that we've had advancement in the definition of accredited investors with more to come so that more people will have an opportunity to invest in private deals. But part of it is simply a dollar amount at the beginning of someone's career. They could be a brilliant new physician, but the fact is she has $300,000 in debt from medical school and only $10,000 to invest, not $50,000 or $100,000. So I think a pool vehicle led by sophisticated investors would provide an opportunity for entrance into the investment field. Thank you.

MS. GARRETT: Thank you, Greg.

MR. SOLOMON: Yeah, one other thing I know we're going to talk about some public market -- later on as well. And certainly, with what's gone on in the public markets in the last few days there's lots to talk about, though I hope we don't get distracted. You know, I do think, though, that a good example when you talk about things like SPACS, because I know we're going to talk about that maybe later on, certainly there's a lot of private placements that go on along with the idea of SPACS.

Certainly, if we talk about the new rules around direct listing, they often talk about financing that comes along with that. Right now, most of those

activities are not really geared towards the kinds of companies who would fall underneath the purview of this office because they're much bigger companies but there's some learning in there to be done.

You know, I can assure you that people, intermediaries like ourselves, would certainly open up the kinds of PIPE offerings and things like that to individual investors but we can't right now because there's just no effective way to get them in under Reg D and the accredited investor rules would make that very difficult. But if there were a streamlined process for us to include individual investors in a safe way that protects them and gives them adequate access to information. I do think that this idea that Greg highlighted is right there for the taking because at the end of the day this is really just about getting individual investors to partner with institutional investors in a way that, you know, gives them a higher probability of making money, there's no guarantees, but a higher probability of having success than not.

And you know, right now with the SPAC craze and everything that's going on as it relates to private to public, right now retail is largely excluded from that capital formation process. Obviously, they can invest in and sometimes do, to their benefit and

detriment in the publicly traded stocks, but there is an opportunity for us to think through things and it's very real as we sit here.

MS. MILLER: Well, Jeff, I think that's a great segue for us to kick into the next segment of our discussion on the public markets and certainly a lot of great ideas and topics that we could potentially take up in future meetings.

So I appreciate everyone's shared excitement over the data in the report. And again, the kudos goes to the entire team for the incredible effort to make it so compelling. So looking forward to the discussion to follow and thank you all for indulging us and if you want to talk a little bit more and ask further questions, encourage anyone listening to join us on February 4th for our Capital Call Event.

MS. GARRETT: Thank you, Martha, and thank you, Jenny and Sebastian for the overview of the annual report. As Martha said, I think we all found that incredibly interesting and look forward to the Capital Call in February.

PULSE OF THE PUBLIC MARKETS

On to the next topic. As the annual report makes clear, public markets play an enormous role in the economy, allowing companies to access capital and broad

pools of investors. The ability to raise large amounts of capital enables critical activities for small companies such as research and development and capital expenditure. Public offerings also provide liquidity to early-stage investors and publicity for the companies' products and services.

It is important that our public capital markets be a place where smaller companies can thrive. But today, fewer companies are choosing to go public as smaller public companies often struggle. Understanding what's behind these issues is important so we've invited representatives from four trading venues to discuss some of the trends and dynamics that they are observing regarding smaller public companies and later-stage private companies that are in the pipeline and how recent innovations are impacting smaller companies interested in accessing the public markets.

I will introduce each of our speakers up front and then they will join us one at a time to share their experiences and perspectives. Committee members should feel free to engage in conversations with them. In addition, following all of their remarks we expect to have time for the committee members to ask questions to all of the guests.

Please welcome first, Martin Alvarez, who is the chief commercial officer of Long Term Stock Exchange, which launched in September 2020. Prior to joining Long Term Stock Exchange, Martin was an investment banker at Piper Jaffray and Morgan Stanley.

We also have with us from the OTC Markets, Cass Sanford, who is the associate general counsel of OTC Markets where she focuses on regulatory and policymaking initiatives. Prior to joining OTC Markets, Cass was an associate at SRF LLP where she focused on capital financing transactions including Reg A+, Reg D, Rule 506(c), and regulation crowdfunding.

From NASDAQ, please welcome Jeff Thomas, who is the senior vice president, head of western U.S. listings in capital markets of NASDAQ, where he oversees new listings in capital markets business. Prior to joining NASDAQ, Jeff held senior positions at SecondMarket, Gerson Lehrman Group, and Altera Corp.

And finally, we have with us today from the New York Stock Exchange, Carolyn Saacke, who is the chief operating officer of capital markets for the New York Stock Exchange Group where she manages sales teams across multiple sectors. Prior to joining the New York Stock Exchange, Carolyn was a managing director at Deloitte & Touche and also worked in the investment banking units at Bear Stearns and Citigroup.

Welcome speakers. We are very happy to have you with us today.

Martin, would you like to begin first?

MR. ALVAREZ: Yes, good morning. My name is Martin Alvarez and I'm the chief commercial officer of LTSE. First, on behalf of my colleagues I'd like to thank the chair and the members of the SEC Small Business Capital Formation Advisory Committee for inviting us to participate in today's panel discussion. So thank you.

The Long Term Stock Exchange is the only U.S. national security exchange with a mission to support companies and investors who share a long-term vision. The exchange offers a public market option that supports long term investment for investors and for companies it provides a multi-stakeholder approach that yields higher levels of innovation and value creation in the future. The exchange features differentiated listing standards that are designed to support listed companies and their mission-aligned investors.

The Long Term Stock Exchange embodies the values of a new generation of founders who aim to advance their vision and build their businesses over decades, as well as investors who want to know not just how companies plan to produce in the next quarter, but

for generations to come. The Exchange also reflects the expectations of employees, customers, suppliers, and communities that count on companies to uphold their commitments and to operate in ways that stockholders in society demand.

The Long Term Stock Exchange received SEC approval in May 2019 and launched last September. In its latest annual report the Office of the Advocate for Small Business Capital Formation calls for continued work on market innovations. It can have the effect of encouraging companies to go and remain public. The Long Term Stock Exchange represents one such innovation. By design, the Exchange aims to address the chronic short-termism that deters companies from going and remaining public and that has been subject of concern among many academics, commentators and market participants.

The series of events over the last 20 years have shifted the public markets to a short-term posture. They range from legal developments such as the repeal of Glass-Steagall Act to the emergence of prime brokerage, a business that is fueled by hedge funds that made public markets the domain of Wall Street, not companies.

Most of the innovation in financial markets has aimed to enhance the ability for traders to profit

from advantages measured in nanoseconds. High-speed trading has nothing to do with fundamental analysis or a company's commitment to creating value over time. The public market that prizes liquidity over long-term value challenges all companies. That includes smaller firms whose shares come to be owned by investors whose focus tend to be on the movement of the share prices, unconnected to the focus by a management on creating long-term value.

These developments, taken together, have led to a reality in which companies, regardless of their size, operate at the periphery of public markets. That has led many companies to sacrifice the creation of long-term value in order to satisfy short-term expectations or to opt out of public markets entirely. The number of exchange-listed companies in the U.S. fell by half in the last 20 years. Over that period the age of companies that go public increased as well. There's a generation of companies that in any other era would be public that have just opted out of the system. And why not? They can raise plenty of money while private.

But chronic short-termism carries with it a number of costs. It limits the breadth of opportunities for investors. Most Americans do not have access to private equity or venture capital and miss out on much of the value creation that happens while companies are still privately held. Their -- stagnate. The same goes for companies' employees who, in many cases, are waiting for their firms to go public to realize the value of stock that provided the bulk of their compensation. It makes public markets the domain of activist investors, high-frequency traders, quants and hedge funds that measure success in 12-week increments or less.

It pushes public companies to prioritize short-term tactics such as buying back stock or managing earnings to meet analysts' quarterly expectations. That may reward short-term investors but comes at the expense of investments and things like innovation, human capital, and sustainability that pay off over years. It creates serious problems for long-term investors and, indeed, for capitalism.

Compared with public markets, the rise of private markets brings with it the cost of greater inefficiencies and opacities. Smaller companies are less able to qualify for late-stage private capital or to bear its costs. And chronic short-termism also undermines economic growth by diminishing investment in innovation and depriving companies of the resources they need to do great things.

So the Long Term Stock Exchange harnesses the

self-regulatory authority of an SEC-registered exchange to offer a way for companies that are actually long term and investors who are actually long term to come together for mutual benefit. The Exchange reflects the belief among many companies that they would be better able to withstand short-term pressures if they were subject to rules that explicitly required them to disclose action promoting a long-term focus. Besides meeting financial and governance thresholds that mirror those of other U.S. exchanges, companies that list on LTSE are required to publish and maintain a series of five policies that focus on long-term strategy, stakeholders, compensation, the board, and long-term investors.

We eschew a prescriptive one-size-fits-all approach in favor of requiring that the long-term policies required by our listing standards reflect five principles. The principles hold that long-term focused companies consider a broad group of stakeholders, measure success in years and decades, align compensation of executives and directors with the creation of long-term value, engage directors in long-term strategy and grant them explicit oversight of the strategy and engage long-term shareholders.

The Long Term Stock Exchange is designed to

offer a listings option for both larger and smaller companies. The listing standards are designed to help companies of all sizes. For example, build bonds with investors who believe in their mission and strategy. Fees to list on the exchange are based solely on market capitalization. For companies with a market capitalization below a billion, for example, the annual fee would be $150,000. We do not contemplate proposing any other fees on issuers such as fees for applications, entry, the listing of additional shares, record-keeping, substitution listings, written interpretations of listing rules, or eRegs.

The Exchange's principle's-based listing standards align companies and investors who believe that business is about creating value for customers and sharing the benefits of that growth with shareholders, stakeholders and society. Of course, a company could just pledge those principles but the problem with pledges alone is that investors have no way of knowing whether the company is serious about honoring them. The Long Term Stock Exchange rests on the idea that companies should commit to these principles by making a binding pledge backed by the authority of an SEC-registered exchange to operationalize each one.

Innovation extends to solutions from the

affiliated LTSE to help companies operationalize long-term strategies by, among other things, enabling them to distinguish investors who are truly long term from those who hold shares for shorter periods. We encourage companies to do a list so that an incumbent exchange would be the primary exchange and the -- exchange would be the secondary exchange.

The Long Term Stock Exchange aligns with a generation of founders and leaders of companies who have a very different value system than what's come before. They care a lot about innovation, sustainability, diversity, and equality. They genuinely believe that companies can be a force to change the worlds for better. They treat all of their stakeholders, including employees, customers, suppliers, communities, and the environment as first-class members of their decision-making process so we can return companies and their long-term stakeholders to the center of the capital markets, and by doing so, deliver on the promise of business and capital to help solve the world's biggest problems and to produce positive change. Thank you.

MS. GARRETT: Thank you very much, Martin. If nobody has any questions for Martin right now, we'll move on to Cass.

Cass, welcome, we look forward to hearing from

you from the OTC Markets.
MS. SANFORD: Thank you, Carla.
I'm just going to share my presentation here. -- everyone can see. I just would like to start by thanking the Commissioners, as well as Martha and her team, and the committee members for inviting us to join this great conversation today.
I'll start with an overview of OTC Markets Group and how our markets operate as not everyone is always familiar with how we operate. OTC Markets Group operates the trading venues for equity securities that are traded over-the-counter, otherwise equity securities not listed on a stock exchange. We operate alternative trading systems that operate as interdealer quotation systems, that's our regulatory status of the trading systems we operate. There's a little over 11,000 securities that are traded on our platforms by FINRA-regulated broker dealers and that includes a wide universe of companies from large international companies to small domestic companies that we'll focus on today.
A few distinguishing features of our markets to keep in mind. One, the market structure that we operate is a dealer market, which means that our markets are really serving as a platform for broker dealers to communicate with one another, publish quotations, and

submit bid and ask or prices in OTC equity securities and then negotiate on these agreed upon prices amongst themselves. This is distinguished from the more common exchange, centralized limit order book or matching engine where orders are submitted to a centralized exchange and matched. This dealer market that we operate does tend to work really well for small companies and those companies with more thinly-traded securities.
Second, these small companies really use our markets as a venture market where the disclosure is streamlined to their type of business and the compliance cost for being public are lower than that on an exchange. So we see approximately 60 to 80 companies every year actually graduate from our markets to a full exchange listing and we're very happy to see that and see the companies successfully go through a public company growth cycle from our markets to an exchange listing. I think last year we had 68 companies graduate to NASDAQ or New York Stock Exchange.
So within this universe of 11,000 securities we organize this large group of securities into different market tiers depending on the disclosure availability that companies provide to the markets and whether they're meeting certain distinct financial

standards. So those market tiers are at the top, the OTCQX market; then the OTCQB market, our venture market; and then the Pink Open Market.
Those two top tiers, the OTCQX market and the OTCQB market really operate akin to a listed market in that companies apply with us and go through an application and review process and are approved before they are admitted to training. So they need to meet disclosure standards, corporate governance standards, and minimum financial standards to be on those markets.
The QX market has approximately 450 companies traded on that market and it's really designed for more established public companies. So this is where you'll see a lot of the larger international companies, including some household names like Heineken, Adidas, and Roche, and then more established smaller public companies in the U.S., a lot of community banks trade on this market. And the financial standards are a bit higher here and disclosure is required of all of these companies which includes, of course, annual reports, quarterly reports, and audited financials.
The next market down, the OTCQB Venture Market, we have approximately 900 companies on that market. And this market maintains the same disclosure standards as our OTCQB market with slightly lower

financial standards as it's really targeted to have -- to be available to earlier-stage companies who are just starting to learn how to be public.
And the Pink market is really our open market designed, again, as a broker's market where brokers can trade securities and quote securities, a wide range, in a regulated way with other brokers. And so this market includes all types of securities which we categorize based on the availability of public information in that market, so we mark securities as either being current, limited, or having no information so brokers and investors can have more insight into the availability of information on companies on that market.
So looking at the -- just those two top markets, OTCQX and OTCQB, where there's collectively around 1,400 companies on those markets, a good chunk of that is really made up of this category of small public companies based in the U.S. So there's approximately 550-plus small public companies here that are traded on these top two markets. And it's helpful to kind of get a look at what these companies look like and understand, as a profile, the types of companies and their demographics.
So we're seeing on average, you can see on the right-hand, this side, these are 50 million market cap

companies, $65 million in annual revenue on average, around 200 employees per company. As far as industry, we're seeing a wide range of industries represented in this 500-plus group of companies. A little over a quarter are from the financial services industry and that includes, as I referenced earlier, a number of community banks, about 100 on these two markets, that have really -- we've found that these companies have migrated to our markets a lot after the JOBS Act allowed them to deregister and delist from an exchange and they can actually leverage their bank reporting as one of our modified reporting standards on the OTCQX and OTCQB markets. So that makes up a good chunk of that kind of 27 percent financial services that you're seeing there.

Then we have a strong representation in the technology industry as well and then a good mix through manufacturing, health industry, which includes a number of biotech and pharmaceutical companies, a good amount of natural resources companies, and metals and mining, as well as other industries. Important to note, these companies are also fairly diverse as far as geographically speaking, hailing from 36 states. So we do see a good amount of companies that are coming from the middle of country and, collectively, these companies are impactful in that they're employing around close to

90,000 employees. So this is a significant group here that's caught within this bucket of small public companies.

So now that we have an understanding of the profile of this public company that's traded on our markets, how do these companies become public? So one thing to note is that companies do not IPO onto the OTC market in the way that they might onto an exchange and raise capital and issue new shares to be listed. A common way that companies do come to our market is through what we now know of what has become increasingly popular on an exchange as a direct-listing-type process. More companies are taking shares that were issued in private capital rounds, making those shares freely tradeable and then publishing disclosure in accordance with applicable rules to then develop a public trading market on the OTCQX and OTCQB markets.

So from the issuer's perspective, I'll use the community bank example again, is that what this looks like is a CEO or CFO of a small privately-held bank, we hear this story all the time, starts to hear -- get phone calls from their shareholders asking is there a public market, how am I able to sell my shares at a fair-market value. And so this process really allows them to provide that liquidity option and public-trading

price to their shareholders at a lower cost than being listed on an exchange, and also illustrates the kind of -- that we operate in a bridge between this private market space and the public markets, so this is a nice pathway here.

Now, as illustrated on earlier slide, the types of regulations that apply to companies on our markets are -- really make up quite a patchwork. So we are focused on really digging into each and every applicable regulation that may apply to companies on our markets. One of the most important that I referenced earlier is Rule 12g3-2(b), sorry, Rule 15c2-11, which was recently amended by the Commission in September and the amendments to that rule go in effect September of this year. And that really shifts and modernizes the way that our markets operate in that it's going to require, going forward, public information from any company that -- in order to be quoted on our markets. So what that really means is it's recognizing the public disclosure that a lot of these OTCQX and OTCQB companies are already providing.

There's a host of other regulations that I'm happy to get into if anyone has questions or if this comes up in the discussion, but as a general matter, we are focused when we look at the office's primary goals

of really improving the public markets for small public companies and encouraging private companies to go public. What our focus is on is improving the existing markets that are serving these companies today, improving the whole process and experience of being public for these companies and encouraging others to do so by making these public markets -- incentivizing companies to join them.

So I will stop for now. If there's any questions, if not can turn it over to Jeff.

MS. GARRETT: Thank you, Cass, for that presentation. That was very interesting.

We're going to go ahead with each of the speakers and we're going to save the questions for everybody for the end, so all of our speakers have a chance to speak.

Jeff from NASDAQ; are you ready?

MR. THOMAS: I'm ready. Thanks, Carla.

MS. GARRETT: Thank you.

MR. THOMAS: So, first of all, thanks to the chair and the committee and the staff. Congrats on the annual report, it really provided some great information there.

As many of you know, NASDAQ is a global technology company serving the capital markets, best known for our U.S. listing venue.

At the end of 2020, out of our 3,500 U.S. listed companies 11,000 had a market cap of under 250 million. So the work of this committee is extremely important for our business and the public markets in general. So we thank you all for your thoughtful service. Of that a third are healthcare companies driving critical innovations to deliver new therapies, methods of care, during this challenging time.

NASDAQ seeks to provide solutions to companies at every stage of their lifecycle. At the earliest stage, about six years ago we launched a non-profit, the NASDAQ Entrepreneurial Center, which provide free education and resources to early-stage founders. And last year we established the Institute for Equitable Entrepreneurship to conduct research on how our capital markets are serving underrepresented founds, in particular, how minority and women-owned businesses face less access to capital than their peers. So I'd like to commend Commission on their work in tackling this topic, not only during your meeting last summer but also the highlights during the annual report this year and we'd welcome the opportunity to share more information on the Entrepreneurial Center's work.

We also launched the NASDAQ Private Market

about six years ago to deal with the challenge of more companies staying private longer. As was highlighted earlier, private companies face challenges in terms of providing liquidity, especially to their employee shareholders, but I'm happy to report that since the NASDAQ Private Market launched, we've facilitated over 450 liquidity programs providing over $30 billion in liquidity to, largely, employee shareholders.

And finally, of course, we have our listing venue for public companies where in 2020 we welcomed 84 percent of all the operating company IPOs in the U.S. Due to the fact that we offer a differentiated value proposition around our investments in investor relations, governance, and now ESG offerings to help our listed companies be the best public companies they can.

The work of this committee really aligns with the journey that we've been on over the last few years under our new CEO, Adena Friedman. When she took her seat as CEO in 2017, we launched an initiative called “Revitalize,” which provides specific recommendations to help eliminate barriers for companies seeking to join the public markets. Small cap companies especially, you know, faced outside burdens in terms of the regulatory burdens of being a public company as well as fragmented and potentially volatile trading and I look forward to

sharing a few of our thoughts on how we can improve that.

We have worked closely with the Commission over the past few years and have seen great momentum on some key initiatives. We want to commend the Commission for their focus on capital formation while balancing investor protection.

So first, I want to give a quick update. As many know, 2020 was a banner year for IPOs. We had 316 IPOs on NASDAQ in 2020 raising more than $80 billion, the most of any U.S. exchange. And there was activity across all sectors, sizes, including small cap growth companies. This year is off to an even faster start. We've already had 91 IPOs that have completed an IPO on NASDAQ raising over 26 billion in proceeds. Now, importantly to note, of those 91 IPOs, 66 have been SPACs, which we have spoken about a little bit already today, but there have been 24 operating companies that have raised over $11 billion this year. So truly a phenomenal start to the year.

If we look back to 2020, of the 316 IPOs, 128 were for companies with a market cap of less than 250 million on their first day of trading. Now of that, those were 89 SPACs and 39 operating companies. So when you look at the operating companies in IPOs, they raised

on average 25 million for a total of 1 billion in capital for those smaller -- companies. And as you look at those 39 operating companies, 18 of them were in the healthcare sector which are, again, helping to drive critical innovations at this important time.

When we think about the reasons why companies are delaying joining the public markets, there are many reasons, but one thing that was noted in the annual report, of course, is the growth of later-stage venture capital. -- actually out here in Silicon Valley, companies in the technology area have outsized access to capital and therefore needs for additional liquidity solutions. However, we have seen with the rise of SPACs, a new path for some of those companies to go earlier in their lifecycle and I'll share a few of our thoughts on why.

When we think about some of the challenges facing smaller companies, one thing we consistently hear from issuers is the increased cost of director an officer insurance and that that inordinately affects small cap companies. So that's one issue we really think could, you know, create -- we could have some room for innovation -- some change on. Also, as I mentioned, the disclosure and reporting requirements for small cap companies given their limited in-house resources can often present a challenge.

The growth, in terms of the requirements around rankers, raters, and different frameworks requiring ESG disclosures, is especially challenging for small and micro-cap companies when they have to think about how to prioritize that versus the other areas. And then they also can face challenges around board recruitment, especially when they're seeking to recruit diverse directors onto a small cap board. So those are all some of the challenges that we're seeking to help companies with.

We talked a little bit about SPACs, but in 2020, of the 132 SPACs that went public on NASDAQ they raised over $30 billion in capital. Now about two-thirds of those were less than 250 in market cap -- public, but it's important to note that a SPAC is typically going to seek a target that is three to four times larger than the SPAC and maybe even larger with the growth of the PIPE market. So one of the reasons we see advantages for SPACs to be advantageous for earlier-stage companies to public is the fact that the companies can provide projections in connection with the merger with a SPAC versus in an IPO only being able to provide historical financials. So that may be one area we want to investigate if there's some way to normalize that to

allow earlier-stage companies to have that benefit.

As we think about other trends and innovations in terms of what's going on with smaller public companies these days, there's really a changing landscape around investor engagement. So, obviously, with everybody working from home the engagement with investors has shifted away from in-person to virtual, but there has also been seismic changes driven by some regulations, like MiFD II in Europe, that have really led to companies having to take on more of the burden of their investor relation strategies in-house and requiring additional strategy tools in technologies to help them engage with investors in a meaningful way.

The other big shift from the IR standpoint is, of course, the focus on environmental social and governance disclosure. So over the past 12 months we've really seen many more companies asking for help in terms of how do they tackle this, in terms of how do they determine which metrics are appropriate to be reporting on and how do they operationalize that so they can do it in a -- way.

Now I would like to speak a little bit about some of the success we've found through our efforts under the Revitalize banner working with the Commission over the past several years. We're extremely proud of

the progress that's been made, specifically the Commission's action around proxy reform to really rein in the proxy advisory firms to provide more transparent, accurate, and complete information around the recommendations they make on voting decisions; the increase around the definition for smaller reporting companies and the scale disclosure that comes with that; the enhancements to the shareholder proposal process, which allows companies to have a more modern way to engage with their shareholders who are looking to put proposals in their proxy; as well as our work with our listed companies to share the community's feedback on the SEC's proposal around reducing the amount of disclosure under 13f.

NASDAQ, in our letter, stated that we believe that this disclosure, in terms of raising the bar from 100 million to 3.5 billion over -- investment managers that would need to report under 13f would dramatically hurt small and micro-cap companies, many of whom signed our letter. We also think, given the topics of today's or this week's trading, you know, we'd like to revisit the proposal we made back in 2015 that short disclosure should be reconsidered and requiring shorts to disclose their positions alongside long investors on the 13f form.

We've heard a number of times today about the challenges around liquidity and trading and the trading environment facing small-cap issuers. In 2019 the SEC invited exchanges and other market participants to submit innovative proposals to improve the secondary market for exchange-listed equities. NASDAQ submitted a proposal that would allow for the termination of unlisted trading privileges for smaller-cap companies which would centralize liquidity on a single venue, and we believe create greater -- incentives to create markets in those shares and provide better price discovery. By concentrating this aggregated liquidity into a single exchange, it will allow investors to better source liquidity, enjoy a higher level of transparency and thereby help smaller-cap companies raise capital and have a better trading market.

Additionally, last year we convened a coalition of -- participants to put forth a specific set of recommendations for the SEC to consider around tick sizes. Specifically we recommended a market-based approach where no tick would be wider than a stock's average-quoted spread but there would be a series of six intelligent tick sizes that would be evaluated by the listing exchange on a semi-annual basis. This, again, would allow more liquidity -- pool at those intelligent tick sizes and that would be especially impactful for smaller cap companies who generally have a lower share price. We believe that the flexibility for exchanges to innovate in order to improve the trading of thinly-traded securities and provide incentives to trade in certain stocks is vital for small-cap and micro-cap issuers.

So, in conclusion, we truly appreciate the partnership we've had with the SEC on some of these important topics when we look at small-cap companies. And we look forward to engaging with this committee in the weeks and months and years to come to continue to find innovative solutions to support the public market for these securities.

MS. GARRETT: Thank you very much, Jeff. We appreciate all of that information.

Carolyn from the New York Stock Exchange?

MS. SAACKE: Thank you. Carolyn Saacke from the New York Stock Exchange. And the NYSE is pleased to be part of the discussion today, as we are strongly behind the Commission's efforts to be an advocate for smaller public companies.

As had been mentioned already, the number of public companies on U.S. exchanges is about half what it was 20 years ago, plus the average market cap of those

companies is six time greater than it was 20 years ago. We recognize that smaller companies are the engines of growth, the drivers of job creation, the innovators, and individually they may be small but together they can be a really great and terrific force in the marketplace. We recognize that the larger, more splashy IPOs are the ones getting press coverage but there are actually many small IPOs in the markets over the last few years, and Jeff had mentioned some of them.

Between 2016 and 2020 there have been 178 IPOs for companies below $250 million in market cap in the United States. This excludes SPACs. So for each of those years the number of those IPOs actually represent between 19 and 33 percent of all of the IPOs last -- excuse me, in the market that particular year. Most of these IPOs were in the healthcare sector and they accounted for just about half of them. The remainder of those IPOs were equally disbursed across consumer, financials, technology, and other sectors. And then for comparison, in the overall market, again excluding SPACs, healthcare and technology make up the majority of IPOs there as well, with the other sectors accounting for the rest.

So the NYSE is an active issuer in this market as part of the NYSE Group which includes both the New

York Stock Exchange as well as the NYSE American. NYSE American is traditionally for smaller-cap companies as they have listing standards that better fit those sizes of companies. So the NYSE Group lists 334 companies and with 250 million of market cap or smaller and the NYSE American accounts for 213 of those.

I think to really understand why there are fewer smaller public companies and IPOs we need to understand what investors are looking for when they invest in them. To invest in an IPO an investor is really looking for a forecastable revenue, steady state growth, and many ready area -- excuse me, readiness areas such as compliance, a finance staff that's experienced in closing the books on time, HR, strong management, and a really clear strategic vision of the future. And to get there many companies, because of that, are going to wait until they're a bit larger and be able to provide investors comfort in these and other areas because they recognize it's not just about the IPO but it's about the long-term time as a public company.

As I mentioned earlier, healthcare companies comprise just under half the IPOs of companies of this size. And these companies, often in biotech, are looking to an IPO as another step in financing their research and innovation and, as such, they're often pre-

commercialization and pre-revenue so they don't need to be able to forecast their financials as well as -- as steadily as most other sectors and they're often leanly staffed. They are exception to kind of the rules of what investors typically require, again, because it's another step in their financing. They're expecting to issue more shares in the future as well, it's just a little bit of a different animal.

We also have to consider why companies go public in the first place. Right? In addition to access to capital, companies are looking to go public to provide visibility in order to attract talent, in order to drive growth, and going public requires -- excuse me, provides liquidity for shareholders and provides a potential acquisition currency for these companies as well. Sometimes, you know, that private company that's looking to go public needs to weigh these two factors against each other, weigh the benefits of everything that I had mentioned with some of the costs that had been mentioned earlier in terms of the cost of going public. And I cannot agree more with Jeff on the issue of rising D&O insurance costs for public companies, by the way.

If the benefits that these private firms, when they weigh them, don't outweigh the cost to the expenses they may choose to wait to go public and that's one of the reasons why companies are waiting a little bit longer to do so. But they also have a growing number of options for providing shareholder liquidity, providing capital, et cetera. There are shareholder liquidity options for private companies and many more of them every day. There are many forms of private capital that are easily accessible. Many companies outside of healthcare chose to delay their IPOs as a result until they get larger because of this access to other forms of capital.

Smaller companies also oftentimes have difficulties attracting liquidity and are thinly-traded and that's been mentioned this morning as well. One of the challenges for them is that many investment funds that are actively managed find investing in small companies actually doesn't provide the terms -- excuse me, the returns that they need to cover their efforts in providing analysis and coverage of these companies. Making a significant investment when you're an active investor in these companies will often result in driving up their prices because of thin trading and also to -- it affects then, in turn, their investment returns.

At the NYSE Group, one of the ways that we're supporting smaller companies is through our market

maker's affirmative obligations to be in the market. We're trying to make sure that from day-to-day trading that there's less volatility to reduce those trading issues that I mentioned. Also, much of the equity assets under management, actually, is in the hands of passive investments, ETFs, and mutual funds, and they tend to track the larger-cap company indices. And investors have been rewarded by large caps, powering good index returns in this segment of the market. There is little passive fund investment of these $250-million-size companies and probably even $1 billion and lower. The returns for these, then, have lagged the larger indices and the concentration of investment dollars in the large-cap stocks tends to crowd out some of the investments in anything a little bit smaller.

Another indication or issue for the smaller public companies is how they're perceived in the marketplace. Some investors may look at smaller companies and think they may be more speculative than larger companies as maybe they don't have the same financial controls, maybe they have less experienced management, again, they're less richly staffed and that could be an issue. And this could be reflected in their valuations in reduced investor interest.

This is where the NYSE really wants to be

helpful as well. We seek to make the transition for companies to the public markets much easier and we provide a lot of services to newly public companies in order to do so, and many of our services particularly benefit smaller listed companies. On both the NYSE and NYSE American, for example, we will provide up to four years of investor relation services, such as webhosting of a company's corporate governance website, newswire services, surveillance, data services, whistleblower hotlines, other services that are designed to jump start their lives as public companies.

And so we're not only saving these companies money by providing these services ourselves and working with other partners in order to do that, but we're also improving their relationships with their investor base, helping them get their stories out. They're getting that mission heard and getting some of those thoughts about speculative valuations or issues that may be the case with looking at smaller public companies, just sort of pushing them out to the side because these investors have -- are improving the relationships with the investor base as well as attracting investors at the same time by using these services.

We provide investor access services as well that mostly benefit our smaller listed companies and

helping them get in front of investors in order to drive liquidity. We provide numerous educational forms for all stages and sizes of private companies in order to help them along the private journey -- excuse me, along the journey to becoming large public companies. There are many, many examples of companies that started off very small on one of our markets or elsewhere in the United States that have then grown to much larger companies. We want to make sure that we celebrate those as well, so when looking for suggestions on how to improve, I loved the megaphone discussion earlier this morning and I think we really should take that to shout out successes of some of these other companies.

In addition, for pre-revenue companies we've recently provided a new fee relief program enabling companies to access the NYSE at a lower cost while they continue to grow their businesses. This has gathered a great deal of interest from smaller companies and several are planning to list under these particular options.

You had also mentioned SPACs a few times this morning and what's really interesting about 2020, in particular, is that there's finally that option of three ways to go public. There's traditional IPO, you converge with a SPAC, and then there's the direct listing. The SPACs have enabled access to public markets for companies that historically would have had difficulties going to market. So pre-revenue companies outside of healthcare, for example, would not have been welcomed in the traditional IPO market. Electric vehicles, alternative energy, others that are still in the developmental stages that don't have a way to forecast those financials have been welcomed with open arms by the SPAC market.

The NYSE started listing SPACs in mid-2017 and since then 35 percent of the business combinations completed on the NYSE Group are actually smaller than $1 billion in enterprise value. I think this is really surprising to most people because the SPACs that you see are those larger ones and the companies that they combine with are those that have way more visibility and are splashier. Since 2016 there have actually been 38 business combinations with a market capitalization of less than $250 million. The NYSE American has listed three of those very recently and they are all in the biotech sector as well, so healthcare is definitely a trend for these smaller companies for sure.

The third way companies are going public is via the direct listing. The direct listings that the New York Stock Exchange has listed, Spotify, Slack,

Palantir, and Asana are way larger than anything that we're contemplating in the discussion today. But a direct listing, as you know, is a listing directly on an exchange without an offering, without trading on the OTC first. Unlike an IPO, there's no capital raised here and so many smaller companies are actually looking for capital as they go public, so this is not necessarily an option for them even to look at at the beginning. Plus there's a smaller number of shareholders in these companies when they're listing and they don't have that broad distribution that an IPO actually will allow in terms of allocation to additional investors, so this also makes this less of an option for companies. Yet the NYSE is very encouraged and very pleased about the recent approval to conduct direct listings with capital raises. And we're encouraged by this because maybe this is a way that smaller companies now can take advantage of the direct listing opportunity.

In closing, we applaud this committee's efforts, and we continue to focus on our support of smaller public businesses on our exchanges. There are great stories of success, as we have mentioned, and we would love for those to be applauded. But we thank you again for your time and we thank you for including us in the discussion today.

MS. GARRETT: Thank you very much, Carolyn.

We appreciate all the speakers today. I think we've all learned a lot about each of the exchanges. Does anybody want to start with questions? Okay, while people are thinking of questions, I'll throw a question to the group. It seems like all four of you talked a lot about how your markets are actually very accommodating to small businesses and it seems like there have been, you know, you all talked about how small businesses are on your exchanges, however, I think we know that less private companies are going public. So I guess I'd like to hear a little bit about more of the risk and the negative sides you see about why small businesses aren't going public instead of, you know, how there is a platform for them to go public. If anybody wants to jump in on that question, that would be great.

MR. THOMAS: I'll start. You know, I think when we talk to -- smaller company, I think it really is a question of, you know, geography, as well as sector and I think that was something that was well-highlighted in the annual report. You know, if you're based on the coasts and you have access to venture capital then really, it's not as much that the companies that been avoiding the public markets, but they just have a better alternative in terms of a relatively cheap form of

capital through the venture capital arena.

As you look at other companies that don't have that access to the later-stage venture capital, then I do think that, you know, there is this issue that martin talked about a little bit which is the concerns around the focus on short-termism in the markets. That's a lot of what we talked about in our Revitalize proposals, how do you encourage more long-term thinking in the public -- markets and so that's one area, I think, that, you know, does give companies some pause.

And then I think, you know, as we talked about before, you know, the trading of, you know, thinly-traded securities continues to be an issue and one where I think we're going to need to provide additional innovations in terms of market structure and incentives so that you can see more liquid trading in these small-cap companies. I think that always has a direct correlation on the cost of capital that these companies will face as public companies.

MR. ALVAREZ: If I were to add a little bit there. I agree a lot -- with a lot of what Jeff shared there. You know, a major theme that's throughout this panel and this discussion is innovation. And there's been a lot of innovation in the markets, but they've been really -- it's really been focused on optimizing for transactions and optimizing for liquidity that is much more related to average daily trading volume, which is one definition of liquidity as opposed to capital access.

So I think that the pain point that especially smaller companies are experiencing are not necessarily being addressed. I think that pain points around transparency into the market, understanding who your investors are, I agree with Jeff around the 13f requirements and how that can really create a whole lot less transparency for smaller companies to be able to see who their public investors are, and their new partners are in the public markets. I think that's critical.

But a lot of where we're trying to innovate is in and around not just optimizing for a successful transaction, like an IPO, but trying to help optimize for being a successful public company. Those are two very different things. So while we might have a fair amount of support, and it's good support, around investor access, companies need a little bit more than that. I think they need to understand, you know, the investor landscape at a little more of a granular level. How long-term are these investors behaving and how do I partner with them?

So we're really focused on innovating, not only to be part of optimizing transactions but for everything in between.

MS. SANFORD: I can also just jump in and want to support Martin's point about looking at liquidity under kind of a different lens. The way that we see liquidity as well is not necessarily in terms of amount of volume transacted, particularly on the OTC Market, but actual ability to liquidate securities, meaning to transfer them successfully and efficiently in between market participants.

So when we're looking at issues that companies have with liquidity, often it's not necessarily just a volume issue but actually back-office compliance issues that are a result of often just outdated regulations, whether that's guidance to broker dealers, transfer agents, and clearing firms on how to safely process securities of small companies. These companies are meeting disclosure standards, they're meeting minimum financial standards, and often the securities transactions are still getting blocked due to outdated guidance and that is, essentially, a component of a liquidity concern too.

MS. GARRETT: Thank you. I appreciate those comments and answers. Sara, did you have a question for

the group?

MS. HANKS: Yeah, I loved the specificity of Cass's wish list and I wondered if the other exchanges would like to sort of follow that kind of in a rules that we -- what is the wish list of each of them, especially with respect to small companies. What maybe, you know, top three things are on their wish list that they would like changed in terms of regulation.

MR. THOMAS: I'll go ahead and start. I'd highlight our proposal around the elimination of unlisted trading privileges as well as our proposal around intelligent tick sizes.

I saw a question for that in the chat and so I can speak for those two for just another minute if that's helpful. But you know, when you think about unlisted trading privileges, right, that the U.S. markets are highly connected and highly efficient, but when you look at the incentives for market makers, especially in small-cap stocks, there's not good economics for them to create that liquidity for the smaller issuers when they have to spread it across so many different venues.

We also see a larger portion of trading volumes for lower-priced securities and smaller-cap stocks occurring in the dark, so not on lit venues,

within the capital markets. We truly believe that liquidity on lit venues is what creates price formation and therefore capital formation and so by centralizing the liquidity for small-cap stocks that would opt-in to this, it would provide the ability for all that transparent -- liquidity to happen on a transparent platform on a lit exchange and therefore we would create more incentives to create liquidity there.

When we think about intelligent tick size proposal, you know, the fact that tick sizes are a penny dates back, you know, to the late 90's. And you know as you look at it, many stocks, especially smaller-priced stocks, are what we call -- tick constrained. So especially a lower-priced stock, the penny is actually wider on a percentage basis than it would be, for example, the very high-priced stocks that we see in the market today due to lack of stock splits. We can talk about those, those are primarily large cap, separately. So by intelligently creating different dynamic tick sizes, which is the intervals in which you see quotes, you would aggregate and pull more liquidity and investor interest around those different tick sizes, which could help both for tick constrained as well as for stocks with wider spreads.

The SEC did run a test in terms of widening some stock's tick sizes to a nickel. In that situation the securities were selected at random in terms of which ones would have larger tick sizes and smaller tick sizes. We think that based on the work the exchanges did to implement that test you could actually now go back, leverage a lot of that investment, and relatively easily put in place an intelligent tick size regime, similar to what they have in Europe and in Asia, where the exchange would look at the average spread for a listed security and then set intelligent tick size to be the smallest increment below that. So no spreads would be widened but it would then create more liquidity at those different bands.

So I'd say those are really the two areas we think that would help facilitate both the trading as well as the liquidity for small-cap companies.

MS. GARRETT: Carolyn, did you have --

MS. SAACKE: Yes, I was about to jump in. Thank you.

I think from our perspective we certainly would like to see the 13f process improved a bit in terms of the recent policy. We believe that some of the, you know, essentially moving and shifting to only having the much larger ones reporting really does hurt the smaller companies. We would like to see that move

forward.

We'd also like to see some review of the quarterly reporting and guidance requirements for smaller companies as well. These are smaller companies with smaller staff and reporting alone takes a lot of time for them to do so and, as has been mentioned, it tends to focus on a shorter-term view of the future versus something in the longer term.

And then also a review of some of the costs involved in going public. And this is going to be an ongoing issue, I'm sure, D&O insurance being just one of them, but it's certainly something that could be helpful and beneficial to smaller companies if there was a little bit more of a manageable cost from their perspective. If you're a much larger company going public and you look at what the percentage of your IPO expenses are relative to what your expenses are in G&A overall, it's not that big of a -- you know, as much of a burden as if you were a much, much smaller company. The accounting may be a little bit more complicated for the larger firms, but you still have to go through all of the audits, you still have to go through the same rigor for smaller companies than you do the other ones and so that's a big one as well.

MS. GARRETT: Thank you.

MR. ALVAREZ: I'd echo some of what was shared by Carolyn and Jeff there. I think the cost of being public is a significant burden, it can range anywhere from $5 million to $10 million a year just to be public. So it's pretty significant.

I think what I'd add on the 13f disclosures is in addition to not limiting the number of investors that are eligible too but considering the fact that there's about 135-day lag time between a company, you know, being able to receive those 13f reports. So I think being able to expedite that a bit would be helpful. It would help enhance transparency. A number of investors list in stock and in street name so it's harder for companies to understand who the beneficial owners of their stock are. So being able to have a little bit more transparency in that respect, I think, I would certainly benefit the companies as well.

MS. SANFORD: I won't go through my full list here, but I do want to just throw our support in as well for extending 13f obligations to OTC-traded companies currently and under the proposal as it was presented. OTC companies, including some very, very large international companies are not included as reportable securities so not only does that harm international smaller companies, but it also doesn't make sense really

that these larger holdings wouldn't be included.

And then just quickly I want to respond to Jeff's proposal and NASDAQ's proposal related to suspending unlisted trading privileges. And there are some downsides to that proposal with respect to just mandating a very prescriptive market structure for thinly-traded securities that needs to be studied a bit further before any sort of venture model is prescribed to thinly-traded companies.

Again, we take the position that we should fix the markets that we have today, fix the plumbing and the various regulations that apply before creating a new model. But there's also just -- there's not enough studying and data done around the conclusion that consolidating liquidity on one venue will actually work to improve trading for these securities.

MS. GARRETT: Okay. Thank you.

MR. THOMAS: Building on some of the comments around 13f, I did want to highlight, I just put up in the chat original petition around short disclosure. So, again, I think that's an important thing for the committee to consider as well. And then I also put up in the chat some of the work we've done around the intelligent ticks as well as the liquidity consolidation.

MS. GARRETT: Thank you, Jeff.

Greg, I see you have a question.

MR. YADLEY: Yeah. This has all been really helpful. I just wanted to ask Martin maybe you could tell us a little bit more about the companies on the Long Term Stock Exchange, numbers and industries and what are the most recent trends you're seeing in terms of companies appreciating how what you're doing aligns with sustainability and on some of the other governance trends.

MR. ALVAREZ: Thank you. I appreciate the question. So as you mentioned earlier, we just went live in the 3rd quarter of 2020 and that gave us the ability at that point to be able to start working with companies around their listings decision and listings venue. The way we're working with companies is in a dual-listing capacity, so they are choosing one of our -- the incumbents here and ourselves where the, you know, we would be the secondary exchange there.

Our primary focus is not really on trading, it's much more around creating much -- a better alignment between companies and investors and aligning incentives from a long-term vision perspective in creating that value. So we're more of a -- think of it more of an operating system that helps optimize a public

market experience for a company. It's compatible with other exchanges, it's compatible with other stakeholders in the market.

From a -- in terms of a differentiation, we have five listings principles and the one where -- that's getting a lot of attention, is very topical, is part of your question which is around ESG and stakeholder capitalism. So we have a -- we require companies to publish a policy that aligns with our long-term stakeholder principle. So we want companies to consider and identify who their broader set of stakeholders are, what types of metrics from an ESG perspective, because we believe ESG is a core component of stakeholder capitalism. And doing it through an exchange really helps create authenticity through accountability because it's different than making a pledge of, you know, or a commitment, it's elevating it to the level of a listing standard that an SRO has oversight of.

So we believe that that trend of stakeholder capitalism is here to stay. It's building momentum. Just look at the fund flows going into ESG-dedicated funds, I believe it is over $13 trillion of assets under management dedicated to U.S. ESG funds these days. So we're here to really accelerate that trend and help

companies be more authentic through accountability with their employees and their customers and stakeholders.

MS. GARRETT: Thank you, Martin.

Jason, did you have a question?

MR. SEATS: Yeah, I've got a question. So when you called for questions, Carla, and then you kind of filled the space, I think you asked a question that maybe a lot of us were thinking or at least my version of the question which is, I still feel like I'm craving a simpler narrative around the market dynamic that we see. And like as -- in general, everyone is observing smaller number of companies being publicly listed, difficulty with smaller businesses accessing those markets. And when you zoom in, all of you have described in detail the regulatory challenges or the changes in behavior of venture capital or the changes in behavior of the public market investors, et cetera, et cetera.

And it's like lots of little reasons, but I just still don't know that I feel like I have an understanding of the macro driver. And I'm seeking that simpler explanation and I'm wondering, and this is an opinion, question, open for opinion here, if the regulatory drivers are the main drivers or if there -- if the bigger drivers are non-regulatory-related things.

In other words, just the competitive dynamics of really large businesses that have network effects and competitive advantages over small businesses and that is a very different thing to try to address than fixing the listing requirements and the overhead for reporting or whatever. And so I would love to just try to get like the simpler commentary from you all on like what's happening. Like why is the public market shrinking in terms of number of listings and concentrating value to fewer larger companies?

MS. SAACKE: That is such a great question because it's so difficult to answer. Right? Because it is such a large -- there are so many reasons. On the positive side, smaller companies have so many more options in terms of finance, more options out there for capital for growth, for, you know, liquidity for their shareholders, et cetera. They have maybe an eye on the prize and just going to do it sometime further down the road or maybe they'll go the SPAC route. We just don't know.

On the other side, there's so many players in it so how do you -- do you fix them all at once? That's difficult. And so from those players, think about, you know, you've got banks, banks are looking at -- they want to do larger transactions because the institutional investors that they're selling to tend to want to be part of a little bit larger of a transaction. Right? So if you're under $100 million in terms of an offering size and you want to be a real player in that, you're probably then going to take a bigger piece from a percentage perspective. You don't want to be a little sliver of a player because you still have to put someone on there to analyze it, you still have all the resources, you've got to -- you want to make sure that the stock is well-traded so that when you do get in and out, because there's a cost there, you want to make sure you can get in and out really cheaply.

And so all of this stuff is tied together. It's tied into if the banks aren't involved doing that type of underwriting, how are these smaller companies getting research? And there's a whole, you know, other discussion we can go deep in the rabbit hole on in terms of how to get research, is it paid research, is it research from the, you know, underwriters, et cetera. So it is such a large question to answer. I think it would be so wonderful if we could give you a simple one and then we could have a 15-minute meeting and, you know, be successful, have an amazing report, and call it a day.

But this is what makes it so interesting,

right? And so everyone on this call are from all different sizes of exchanges and trading venues that are all looking at it in a different manner but all trying to get more of these smaller companies going public because we need more public companies. We recognize that these smaller companies are just the drivers of innovation and jobs and all of that. Looking at the numbers of jobs of the companies in the report, if you took that percentage of like a company's market cap, for example, and you said, "Okay, this many companies under $250 million are creating this many jobs," if you looked at a large company with that same market cap there's no way they're coming near that job creation. And I think we all recognize that and are trying to save it, but I just wish I had a better answer for you.

MR. SEATS: Well, I appreciate the complexity of it. Maybe I'll ask a more direct, specific question. In your opinion, Carolyn, all of the factors that would be covered under regulatory oversight, so the things that could be influenced or modified or controlled by this group of people and by the Commission, is that -- factor a larger driver or a smaller driver than all of the other factors that are just market factors and things that are non-regulatory in nature?

MS. SAACKE: It's a large driver. I don't

think it's the largest driver out there because, again, you do have those positive, you know, other access to capital and things like that, but it can make a significant change.

MR. THOMAS: So, Jason, I'll provide a little bit more of a macro thought. So some of the macro trends in the asset management industry have been the shift from active to passive investment. With the rise of ETF and index funds you've seen fee compression on asset managers and so that's reduced their ability to play an active role.

At the same time, as you saw more and more companies waiting longer to go public, that shifted the focus for those active managers from the public to the private markets to generate alpha. And so you look at those two big factors, as the public markets become more focused around passive or indexed investment and the asset managers shift from public to private, one of the side effects of that, and I think Mr. Solomon mentioned this pretty well, but you all of a sudden fall into the regulations that limit retail's participation in those private markets and so I think that also has an impact. Right?

If you take a big segment of the investing public out of the opportunities that's going to, of

course, affect companies' access to capital and so I do think that that's one area to look at. Right? As things are shifting from active to passive and from public to private, that's where I think we have to make sure that everybody is included in the opportunity to have the prosperity.

And then, of course, the other big macro factor that we haven't really talked about, but since the financial crisis we've been in a very low interest rate environment. And so then when you kind of look at the cost of equity versus debt it really changes those dynamics as well. So, again, I don't think it answers your question about what's more important, but I do think it's important to keep an eye on the macro drivers of the asset management industry while trying to solve this issue.

MR. ALVAREZ: If I were to give a shot at maybe simplifying a little bit from our perspective. Sometimes, you know, you got to be able to call something out to get past the complexity and one of the things that we've seen, and I'll post it in the chat, I put together a piece that went through six areas -- six things that really catalyzed how this market transitioned. So it's ironic that it took about 20, 25 years, so long-term play, for the market to shift to such a short-term posture.

And to get to your question, it used to be that companies were at the center of the capital markets and now they're at the periphery. So when we talk about all the options that are available for smaller companies, those options are really driven off of the dynamic that the market works much better for larger companies because now you've got, instead of companies at the center of the capital markets and capitalism you've got investors, especially investors that are facilitating the type of liquidity on a daily basis, and those investors want companies of a certain type. And that doesn't lend itself towards a healthier environment for some of the smaller companies.

So when you look at those options, SPACs is a great example. SPACs used to be, because they've been around since the mid to late 90's, for companies that couldn't go public in a traditional format. And that's why SPACS have structural features like warrants which tend to translate into a significant amount of hedging activity in the markets and those warrants are there to help mitigate risks that investors see in companies that have traditionally gone public through a SPAC. So you have a market environment operating within a regulatory framework that is leveraging that framework in a way

that is much more conducive to larger companies.

So just look at the facts, look at the reflection of the market. Fewer and fewer smaller companies, fewer companies that are public, much larger companies because that serves the market better. Jack mentioned passive investing. Passive investing is very supportive of larger companies through index funds and ETFs. So until we can start to shift the narrative a little bit and put companies more back to the center of the capital markets, we're going to keep going through the kind of mental gymnastics of coming up with options for smaller companies because the market is optimized for larger companies and trading.

MR. SOLOMON: Yeah, we're going to have to probably bring this to a little bit of a close for lunch. Carla, do you --

MS. GARRETT: Jeff, can we have Cass speak real quick?

MR. SOLOMON: I'm sorry. I'm sorry. I'm sorry, Cass. I didn't know you wanted to speak. My fault.

MS. SANFORD: No problem, Jeff.

No, I just did want to also attempt to answer Jason's question and then get to quickly go over some of the points that Commissioner Peirce mentioned earlier.

But Jason, I really think that there's often a misconception that the private and the public markets are black and white and mutually exclusive when, in fact, there is this middle ground that needs to be examined in how companies go back and forth between them. And I'll give you a quick anecdote to help illustrate that which is that group of 556 small U.S. public companies on our markets that I showed earlier, close to 90 of those companies actually filed a Form D in 2020, so these companies are actually -- they're public, they're traded on our markets and often look to the private markets to raise capital and that's something that we should -- just to illustrate the fact that it's not as black and white as one would think and we need to focus on, I think, improving and making our public markets a little bit more incentivized so that companies are actually raising capital publicly.

And I have a couple of recommendations, one of which as an example, is just improving Reg A to allow for at-the-market offerings or allowing companies to actually sell their shares back into the market in the same way that they might buy them back. So kind of more innovative market-structure concepts but I think that that often gets overlooked as we talk about private markets versus public markets. It's not quite as black

as white as we think.

And then really quickly I also just wanted to address one of the topics that Commissioner Peirce raised which is reform related to transfer agent regulations as well as guidance to broker dealers. And again, this is one of the ways that the public markets, at least from our perspective, can be improved is there's often -- first of all, the transfer regulations have not been revised or updated in many, many years and these market participants do hold a huge wealth of information about share ownership, transfer history, and information that's relevant to Section 5 violations. And so releasing that information by requiring disclosure of the transfer agents would be valuable to the entire ecosystem, broker dealers, clearing firms, as well as issuers.

And then with respect to broker dealer guidance related to transfers of restricted securities, there's just a lot of the regulatory guidance is quite outdated. There's a FINRA notice to broker dealers from 2009 that outlines a number of red flags for facilitating transactions in restricted stock which, again, a lot of these private companies, they have just issued private rounds and have restricted stock, so this is a burden for them to make that stock publicly traded.

That guidance dates back to 2009 and so it does not take into account the types of data that's available now and can be leveraged so that brokers, clearing firms, and transfer agents can look at publicly-traded securities and say, “These are safe, these ones are creating disclosure, I can process these safely in accordance with regulations.”

MS. GARRETT: Thank you, Cass.

Jeff, did you want to speak or --

MR. SOLOMON: Yeah, but if you had a question, go ahead, Carla.

MS. GARRETT: I have a quick question and maybe it's a very micro question, but a lot of you brough up D&O insurance and how the costs are becoming so expensive that private, you know, it's hard for small companies to actually get D&O insurance. I was just wondering if you guys have seen any solutions to that problem.

MR. THOMAS: So it's not relevant to the small cap issuers but some of the larger cap issuers are seeking a change in Delaware state law that would allow them basically to self-insure. Other states, like New Mexico, have that. As you know, there's lots of reasons why companies incorporate in Delaware, but this is one area where, you know, we think the approach could be

changed. So, you know, again, doesn't specifically address what this committee is looking at but it's one of the things we put our voice power in supporting, at least one change there.

I think, you know, it is a very dynamic situation. It's all based, frankly, a lot on the case law and the decisions in the courts. There have recently been a few findings in the courts that are actually, I think, moving things back away from needing to, you know, consider -- and handle things a little bit more federally which I think is where a lot of the challenges come from. But if there's anything that, you know, this committee or the Commission can do to kind of look at how do you, you know, centralize and kind of manage that risk at the federal level as opposed to the state level, that seems to be where a lot of the challenges come from in terms of the pricing of that insurance.

MR. SOLOMON: Can you guys hear me?

MS. GARRETT: Thank you. Jeff, yes.

MR. SOLOMON: Anybody else have a -- anybody else want to respond to that or -- before I just say a few things to answer -- try to summarize some of Jason's question in less than two minutes?

Well, Jason, you did ask the unanswerable,

which is great, and it really shows I think the complexity of some of the challenges we face. And I'll just, you know, I think a lot of us, we spent a fair amount of time on market structure, certainly our experts today are experts on that and, you know, a lot of the challenges I think facing the public markets today just aren't going to change unless there's a wholesale change to the way the public markets are traded in the U.S. We have a market structure here that is -- that we can go into in detail offline. I don't think it's really the purview of this committee, but it definitely impacts capital formation, there's no question about it.

You know, most people still think that there are market makers who take risks trying to make markets for small-cap companies. That hasn't been the case in -- since Reg NMS, for sure, but maybe even before that and that's almost 15 years ago that that primary function of intermediaries standing in between buyers and sellers and taking risk to create liquidity, that doesn't exist anymore. And part of what we're seeing in the market is the friction associated with buyers and sellers just meeting without anybody having to take risk in between the two of them and sometimes it works beautifully and sometimes it doesn't and it can be nasty

and right now we're in one of those nasty periods.

And I know the narrative of what's going on in the world with regards to GameStop and everything like that is an interesting one. And there are lots of stories that will be told about it, but at the end of the day what's it's going to end up being is there will be a lot of congressional hearings about this and market structure will be back in the forefront of a lot of those conversations. I think what we need to think about as a committee is how we keep people focused on the things that are necessary about our market to foster capital formation.

I think we're all going to get a chance to say our piece on market structure probably over the next three to six months as there's congressional hearings and it will be really interesting to see how all of our speakers today and their people, you know, respond to it. But we need to make sure that we stay focused on the idea that market structure does impact capital formation, especially for small companies, and if we can be doing things as a group to make recommendations to make that market structure more conducive to capital formation, we should do that.

What those would be and how those might look, it's a tough -- it's tough to give you those answers but a bunch of us have done a lot of work on it over the years including -- I mean we worked very closely with -- actually with everybody on this, all of our speakers today, maybe with the exception of the Long Term Stock Exchange, we should probably spend some more time there with you. But it is definitely something that we'll have to address as a committee as we kind of come up with recommendations for market structures we think will work for small companies.

It's 12:30, I'll turn it back to you, Carla.

MS. GARRETT: Thank you, Jeff, for those comments. And I want to thank our speakers again, Martin, Cass, Jeff, and Carolyn. We really appreciate you being here and sharing your thoughts and comments with the committee. It is now 12:30 and we will break for lunch. We will reconvene at 1:30. The webcast will be stopped during lunch and we will see everyone back at 1:30, so have a great lunch.

(Whereupon a luncheon recess was taken at 12:30 p.m.)

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

MS. GARRETT: Hi, I hereby call the meeting back to order. I hope everyone had a nice lunch.

Martha, a couple of members have asked about the White House memo asking the agencies to consider

postponing effective dates of recently adopted rules. Is there any light that you can shed on what impact that memo would have on some of the rulemaking the committee weighed in on last year?

MS. MILLER: Yeah, Carla, happy to provide some clarity. If the -- as you pointed out, in the things where the SEC took Commission action via rulemaking, if the SEC were to do anything to change any of those amendments that would also need to be done by Commission rulemaking.

COMPENSATORY OFFERINGS FOR WORKERS

MS. GARRETT: Okay. Thank you very much. Okay, to move on to our topic for this afternoon. At our last meeting Kesha mentioned that she would be interested in the committee exploring the topic of workers in the gig economy being able to participate in upside of tech platforms through equity compensation.

And this is a very -- topic because the SEC had been looking at this issue and on November 24, 2020, the Commission proposed rules that on a temporary basis would permit an issuer to provide equity compensation to certain platform workers who provide services available through the issuer's technology-based platform or system. The Commission also proposed rules to amend Securities Act Rule 701 and Form S-8 in order to

modernize the framework for compensatory securities offerings.

Joining us today is the SEC staff member who helped write the proposed rules, Anne Krauskopt, with the Division of Corporate Finance's Office of Chief Counsel. Anne will provide a summary overview of the proposed rules for us today.

Anne, thank you for joining us. Anne, I believe you're on mute so you might want to unmute. There you go.

MS. KRAUSKOPT: I apologize for that. I'm happy to set the table for our discussion today. Of course, any views I express are my own and not necessarily those of other members of the staff or the Commission.

Offers to employees for compensatory purposes are public offerings. They are not eligible for the Section 4(a)(2) exemption, but the Commission has long recognized that offers in sales of securities as compensation are different from capital-raising offerings and they've made special provisions for them.

First of all, Rule 701 for compensatory transactions by non-reporting issuers. This rule is subject to caps on the number of securities that can be issued in a 12-month period. There are specific

disclosure requirements that apply to offerings exceeding $10 million, the securities issued are restricted securities and the offering is not integrated with any other securities offerings.

For reporting companies we have Form S-8, which is an abbreviated registration statement that becomes effective automatically upon filing. There is no prospectus filed with it. Plan documents are used for prospectus delivery and company Exchange Act reports are incorporated by reference. There is no annual limit imposed on the number of securities that can be issued and the securities are free-trading rather than registered.

Now, on account of developments in both the kinds of securities that are issued as compensation and also the developments and evolution of the workplace that you were mentioning, we had a concept release in 2018 which requested comments about what was working, what wasn't working, what we could change, and in November we published two proposing releases trying to synthesize that and make our best recommendations.

The comment period is ongoing. It's extending until February 6th. We haven't received comments yet and we are very eager to hear from you and your colleagues. It's always with the benefit of comments that we can figure out the best way to go.

Looking first at the technical amendments release, a significant topic was 701(e), which requires additional disclosure if the offering exceeds $10 million in a 12-month period. We made a number of proposals about this because it's been a source of difficulties in practice. First, rather than require the additional information to be given to all investors in the offering if it exceeds $10 million, we proposed to require it only for sales after the $10 million threshold is exceeded which would eliminate the possibility of retroactively losing the exemption if it's not delivered to the earlier investors.

We would conform the age of financial statement requirements to those in Form 1-A so that they're available on a semi-annual basis and people would not be required to update them more frequently for compensatory offerings than they do for capital raising. Foreign private issuers eligible for the 12g3-2(b) exemption from Exchange Act registration would be allowed to provide financial statements in compliance with home country accounting without reconciliation to GAAP. And more broadly, we would permit alternative financial disclosure in the form of an Internal Revenue Code Section 409A valuation report.

These would be prepared in accordance with code regs for determining fair market value of stock not readily tradeable on an established securities market. It would require an independent appraisal. The 409A rules are widely used. They have independent significance for tax purposes but for our purpose we would require updating every six months and a delivery of the valuation report.

Another significant topic was restricted stock units. We recognized that since 701 was last amended, these have become a pervasive form of equity compensation. They are a derivative security, but unlike options they don't require an investment decision to exercise but instead settle automatically in the underlying shares when held to maturity. The rule currently provides for derivatives securities that disclosure be given before exercise or conversion, but with RSUs, the relevant investment decision takes place at grant so the obligation to deliver would apply at that time, which raises practical challenges in the context of new hires particularly.

So the proposal provides that if a derivative does not involve a decision to exercise or convert, the obligation to deliver would apply a reasonable period of time before the date of grant. And in the context of

the new hire, the disclosure would be considered delivered at such a time if it is provided no later than 14 days after the date the person begins employment.

The proposal also amends Rule 701(d), which provides three alternative caps that cap the overall amount of securities that can be issued pursuant to 701 under any year. The $1 million cap would be raised to $2 million, the 15 percent of assets would be raised to 25 percent of assets, reflecting that today's businesses are less asset intensive, and the 15 percent of outstanding securities cap would remain the same.

We would expand eligible recipients to some degree. For consultant and advisors we would extend eligibility beyond natural persons to small entities, substantially all of the activities of which involve the performance of services and that are substantially owned by persons who directly perform those services. This would strike a balance between allowing service providers the benefit of organizing as an entity with our need to prevent use of 701 for passive investments.

We would expand former employee eligibility to those issued -- to compensatory securities issued within 12 months following a termination and to former employees of acquired entities in exchange for compensatory securities that were issued by their

target. We would expand the eligibility for S-8 the same way. And with S-8 we would implement other improvements to simplify registration on the form, eliminating unnecessary procedural friction consistent with investor protection, including clarify the ability to add multiple plans to a single form S-8, the ability to allocate securities among multiple incentive plans on a single S-8, and permitting the addition of securities or classes of securities by an automatically effective -- amendment.

We would also implement share counting improvements and fee payments relating to defined contribution plans. One of the problems that we see with 401-K plans and similar plans is the difficulty that plans have in keeping track of the number of shares that have been issued and not running out, where, you know, today you have to register a finite number of shares.

What we propose is registering the offering of an indeterminate number of securities and implementing a new fee payment method that would call for paying 90 days after the end of the plan fiscal year based on how many shares were actually sold. We also would do some revisions that track changes that the IRS has made to their plan review practices reflecting that they no longer review qualified plan amendments and eliminating the requirement to describe the tax effects of the plan on the issuer.

Now, turning to the platform workers. The gig economy, this has been a big development in recent years where we see individuals using an internet platform to find work providing goods or services, not to the company but to third-party customers. An individual who's doing this often has similar relationships with multiple companies doing either the same or in some cases different kinds of work. And given the characteristics of this relationships, the individuals may not fall into the current eligible categories of employees, de facto employees, or consultants, or advisors. So the Commission has proposed temporary rules creating a new category of eligible individual, the platform worker, which would establish conditions for participation.

The same conditions would apply both for 701 and S-8. First, the issuer operates and controls the platform as demonstrated by ability to provide access to the platform, control the terms of service, and the ability to remove workers from the platform. The securities would be issued under a written compensation agreement not in connection with capital raising or

market-making services. The quantity would be capped at no more than 15 percent of the value provided by the worker over a 12-month period and no more than $75,000 over a 36-month period.

The amount and terms of securities issued may not be subject to individual bargaining or the worker's ability to choose between cash and stock and issuers must take reasonable steps to restrict transfer of the securities except to the issuer or by operation of law if issued under 701. And for 701, the issuances for platform workers would fall under the same 701(d) ceiling as the company's issuances to regular employees. There would not be a separate ceiling for platform workers only.

To help the Commission evaluate the operation of the temporary rules, we also proposed to collect information from the companies at 6-month intervals relating to the criteria that they used to establish eligibility. The types and terms of the securities that they're issuing, if under 701, the steps they would take to prohibit the transfer of securities, and information regarding the percentage of overall securities that they're issuing under these temporary rules and how the issuances compare both on an absolute term and percentage basis with the securities that they're

issuing to regular employees.

One thing, particularly, that I want to point out is although we understand that the development of the gig economy raises a number of issues under labor, tax, and other regulatory regimes, our proposed amendments to include these workers in S-8 and 701 reflect solely considerations that are relevant to U.S. securities laws and are not meant and should not be construed to address issues under any other regulatory regime and we express no opinion on whether or not gig economy or platform workers would be considered employees for purposes of other laws or regulations.

So, with that, I'll turn it back to you for a discussion and I will make another pitch to get comment letters in to us so that we can deliver the best final rules that are most appropriate for the problems that we're addressing.

MS. GARRETT: Thank you, Anne, for that summary of those rules.

Does anybody on the committee have any questions or want to comment on this proposal?

MS. CASH: I do but I didn't put my hand in the chat so I'll -- goes first.

MS. GARRETT: Thanks, Kesha.

MS. CASH: Is it okay? I saw someone in the

chat had a comment.

MS. GARRETT: Go ahead, Kesha, and then we'll turn to Brian.

MS. CASH: Great. Thank you, Anne, and we will -- and I say “we” because it's on behalf of my firm, Impact America Fund, we will be commenting and those comments, we'll have those in to you no later than Monday. So we've been looking at the proposals and working through that.

One question we had, kind of taking a step back, would love to hear your thoughts or perspectives on not the reason why because we know the future of work includes many gig workers and we know that typically those people are lower income workers, so we understand the importance of it, but from a philosophical standpoint. Sort of are we thinking about this in terms of sort of a new form of a retirement plan, an opportunity to invest, additional compensation, we'd love to hear thoughts around the philosophy around the proposal.

MS. KRAUSKOPT: Well, I think it remains to be seen what kinds of programs would develop and be offered to gig workers. I think some of that may depend on what they're eligible for under other regimes. For example, 401-K plans and other qualified plans have to comply with the requirements of Section 401 of the Internal Revenue Code and, you know, I'm not prepared to say that gig workers, necessarily, would be able to contribute in those. It depends on what the tax rules say. But I would think that this would be a way to provide the kind of incentive plans that generally are used for employees today.

MS. GARRETT: Kesha, did you want to respond to Anne's answer in any way at this point?

MS. CASH: No, I think I just -- I wanted to pose the question. I think we're, you know, where obviously this is new and there are a lot of things that need to be worked through. I think thinking about, you know, gig workers are here to stay, and I think that the future of work, we have to consider that the gig workers are the new employees in many cases.

And so thinking about I just implemented a 401-K plan for my small firm and that, you know, there are certain kind of rules and regulations around that and I understand that. And for us as a small firm, it's important for us to create a wealth-building mechanism and sort of it's part of the full compensation package. And so I wonder, as we think about gig workers and giving them this possible way of participation beyond their compensation or in -- as part of their

compensation, what's the end goal? What are we actually trying to accomplish by doing that?

MS. KRAUSKOPT: Well, the proposal recognizes, as you say, that gig workers are a significant development in the world of work. That currently, because of how our rules are structured and how the terms are defined that they may not currently be eligible to receive securities as compensation, but we contemplate clearly that these would be compensatory offerings and not offerings for a speculative purpose.

You know, we are concerned, for instance, that you know, some guardrails may be necessary in order to not encourage people to sign up on kind of a spurious basis to enter a gig arrangement just because they want to get stock. That's why we're seeing things like the proposal that it be limited to -- that the number of securities issued to an individual be limited to 15 percent of the value of their services in the year and not more than $75,000 over a 36-month period.

You know, this is an area that is, you know, very new. It is evolving. We don't know how the gig economy is going to work or continue to evolve and, you know, we're proposing this on a temporary basis so that folks can kind of take it for a test drive and see how it works in terms of the objectives of the issuers and

the workers, consistent with investor protection and consistent with it being a compensatory offering.

MS. GARRETT: Thank you. Brian?

MR. LEVEY: Hello. Hi, everyone. Anne, thank you for some really great efforts here. I think, as you mentioned, this is an evolving area, and my sense is the SEC is sort of taking a leadership role here. As you mentioned and acknowledged, the labor laws might not be keeping pace with the SEC's innovative thinking here and I think that could be an issue here for companies and might cause them to hesitate using this going forward, at least until the labor laws are cleared up. And those labor laws, you know, have stayed in effect largely since the aftermath of the Great Depression in the 1930's and they need to evolve over time.

But I think the biggest roadblock for companies in using this sort of stock for platform workers is really -- my understanding, there's federal case law and in some states as well that if a company does offer benefits, which includes stock, that transitions these workers to employee status as opposed to independent contractor status. So that will make it tough.

But there also, I think a majority of the states have what are called ABC Tests, which presume

workers are employees unless the hiring entities can prove all three of the A, B, and C prongs and one of those prongs says that, you know, this person or worker is not part of your ongoing business. And to the extent that you offer stock that you offer to employees, it's harder, I think, for those companies to make that argument.

So, you know, I think it's some great progress. I think, as you said, we'll need to see how this unfolds. I would say that lodging and accommodation platforms such as the Airbnb's of the world, the hosts are not necessarily providing services, in my mind they're providing lodging, which could make it easier to reconcile the SEC's rule here with the labor laws because true services are not necessarily being provided by those lodging hosts. So it will be interesting to see, you know, whether that is one area that sort of, you know, where progress is made as a result of this temporary rule. So just some food for thought.

MS. KRAUSKOPT: Thank you.

MS. GARRETT: Thank you, Brian. That is an interesting perspective with respect to the employment benefits and how that could affect the status of a person's -- whether they're an employee or an independent contractor.

I had a chance to read a couple of the comment letters that are on the SEC website at this point and many of them at this point are from actually the gig workers themselves. And it was interesting to see that some people were very in favor of it and some people were against it. And one of the issues that did get brought up was that this would be an alternative to them getting compensation and that was something that one of the commissioners brought up this morning also. I just wondered if the SEC had considered that.

MS. KRAUSKOPT: Well, you know, what we have proposed is that they not get more than 15 percent of the value of their services and that they not be able to negotiate between getting stock and getting cash. If there are issues revolving around that, those are certainly issues that we would want to hear about through the comment process and consider, you know, carefully at some length as we consider how to go forward.

MS. GARRETT: Thank you. Youngro.

MR. LEE: Thank you. I actually had a question. And I'm not an expert in labor law by any means, so what Brian and Kesha said about how it relates to labor issues, I think that's definitely a big

concern. However, I was just wondering has there been any consideration or possibility of maybe creating a similar concept as, for example, in private funds there's a knowledgeable employee exemption that basically allows different ways for knowledgeable employees to participate. Is there any consideration of possibly using existing offering rules, whether it's Reg D, Reg A, Reg CF and maybe creating a separate, you know, exemption basically for however you want to define it, knowledgeable contractor, knowledgeable affiliate, just to --

MS. KRAUSKOPT: I think that's unlikely. You know, our exemptions are basically designed for different purposes and the ones that you have described relate to capital-raising transactions. The Commission, over the years, has made accommodations that if used as appropriate for compensatory transactions through the rules that we have, both S-8 and 701. And, you know, I think given that there's a certain amount of, you know, creating a design that's consistent with the purpose of the transaction that we're more inclined to build on 701 and S-8 rather than to go off in a different direction that would be building on our capital-raising exemptions.

MR. LEE: Just to clarify, so I completely

understand what you're saying so maybe let me rephrase. Historically, you know, when we think about building wealth it's not just about getting paid, right, it's about investing the right way. And you can argue that the reason the knowledgeable employee exemption and private funds, especially, works because -- insiders. The employees actually know, themselves, much better than anybody else how good their company or their investments might be.

So, example, the early drivers of Uber or early, you know, whatever, participants in Airbnb, I'm pretty sure a lot of them felt like, “Oh my God, this is going to be big.” Right? So if they had a chance to invest their own money into those companies, I'm sure they would like to and from a company's perspective that actually might be also attractive because you're not just giving, right, compensation, you're actually allowing the participants to basically bet on their own company. So that's kind of where -- I completely understand your point in the conversation, but I think just even allowing the opportunity for themselves to invest into these companies and by being a participant they do have a better information.

And it also, you know, kind of philosophically helps in my mind, the wealth-building equation, you

know, to have some ways for people who would otherwise not be able to invest in these rounds to participate, for example. In fact, I think Jeff mentioned this several times, when Uber was doing Series A, it was obviously opened to accredited investors only. If there was exemptions for existing, you know, gig -- Uber drivers to participate in that same round I can imagine a lot of people would have loved to do that.

MS. KRAUSKOPT: Well, if they are accredited investors, they can invest pursuant to the exemptions for capital raising that are based on investors being accredited.

MR. LEE: That's right. So what I'm saying they're -- who are not accredited. So, you know, it's just an idea, just a thought that there is a different angle to this which is a lot of non-accredited investors who are presumably gig employees, if there was another exemption for them to participate from an investment perspective as much as the compensation perspective.

MS. KRAUSKOPT: Well, you know, maybe what they need is a registered offering

MR. LEE: True.

MS. KRAUSKOPT: You know, I just don't see -- I don't see that fitting in the paradigm that we currently have.

MR. LEE: Understood. Thank you.

MS. GARRETT: And Martha, did you have a comment for the --

MS. MILLER: It's more of a question for the committee to use as a springboard as we think about these interrelated concepts of equity compensation for these gig and platform workers. We're talking about compensation, I've also heard Youngro just most recently was saying kind of the wealth-building, that retirement aspect, and then there's also kind of what are the long-term incentives of the employees which relates in with governance questions. I would love thoughts from the committee that can help inform us on how do we strike the right balance.

Anne highlighted that 15 percent threshold that -- 15 percent maximum amount of compensation but how do we align and set up a framework? This is where I think the committee can be particularly valuable with input on how do we align the equity portion of whether we call it compensation or getting a stake or say in how the company is governed or that long-term wealth creation with the cash compensation. That's absolutely critical for most of these employees to still have as a pipeline.

I'd welcome feedback. I don't have anybody in

particular, I would love if anybody wants to weigh in on that question.

MS. GARRETT: Jeff?

MR. SOLOMON: Hey, sorry about the, you know, I'm smiling. I'll smile with my eyes. I'm in a public place so I need to be masked. I think a couple things. First of all, I think it's a very fine line and I'd love to get some feedback from Kesha here because it's a very fine line between how you frame equity compensation or non-cash compensation in the context of a cash compensation. And I just think there's a dynamic in play here that I would worry about a little bit. Meaning that until we establish things like a national minimum wage or a minimum cash compensation that companies must do, I worry about companies using stock or -- that invariably a big chunk of which will be worthless if it's private companies. I mean we just know the math behind private companies, everybody on this phone does but I'm not sure the gig workers do.

But, you know, the idea that people could -- for, you know, big chunks of cash compensation at the expense of -- big chunks of equity compensation at the expense of cash compensation. So I'd like to get a little bit of guidance on what parallel rules we might have in place that make it so that there's a minimum

cash compensation associated with that before this even kicks in, otherwise I just worry about people -- I worry about the untoward who will just, you know, layer in worthless equity and people will be working really hard and they'll have nothing.

So I think the committee should consider giving advice to having a parallel cash compensation structure that has to be met prior to their award of equity or it has to be done in conjunction with the award of equity so we don't have a problem there.

Kesha, I don't know if you've thought about that at all because I'm not sure I'm qualified to sort of opine on that and I just think it would be really helpful to know -- to have your perspective on that as you've had more conversations with people about this than I have.

MS. CASH: Yeah, I think -- I mean I don't know how we get there but I know that financial literacy has to be a part of it. And there needs to be, you know in my opinion, some financial literacy tied to any company participating or issuing stock in this way to said gig workers to ensure that the gig workers have clarity on what they're actually receiving.

There's -- and we'll include this information in our comment letter, but we had an intern, a fellow,

do a case study on Juno which was an Uber-like company that had issued restricted stock units and that company was acquired and the drivers did not get what they thought they would be getting from that. And some of it did have to do with the existing sort of rules and regulations as to why, you know, those restricted stock units were basically worthless with the acquisition and promises that were made, weren't kept. And so I think from that case study, if we're going to do this and do it the right way and it's not a scheme there has to be thoughtfulness around that financial literacy and have that baked into companies being able to participate in this program.

On the flip side of it, because I'm an optimist and I know our job, you know, often is to protect people and to protect their money, which is important to do but I also know that, you know, we're invested in a company that is essentially a platform for hairstylist. And those women -- these women are making more money than they did prior to being a part of the company we're invested in and, you know, kind of our thinking around that and we got here as to where the rules and rulemaking is happening in regard to that 2018 proposal, from doing our research.

These are gig workers, but they are so

valuable to our company that the founder would, indeed, like to have them share -- they're sharing in the income of the company, could they share in the actual equity participation and can they have a choice in that. Right? If I owe you, you know, $1,000 for the services that you provided, do you have a choice to take that as cash compensation or as equity? Having clarify of choice is important but I think when we talk about economic -- and wealth building, oftentimes low income populations haven't had access and then they don't have a choice when they do have access.

MR. SOLOMON: So that's an interesting concept that I think we should think about, you know, maybe advising what you said, the optionality of it. And I think you mentioned that earlier but it's worth mentioning here that it's not so much prescriptive as it is optionality, that there has to be training and understanding of what the risks are associated with taking equity options as a percentage of your compensation and that there should be optionality to it.

And I think that we should build that into the rules so we don't have employers that simply use the rules as a way to suboptimize cash compensation. And a lot of the companies are going to be cash-strapped by nature and they will use equity compensation because

effectively it helps them to have a longer cash burn and we just want to make sure that that equity actually has value down the road.

But I think we also have to educate people that equity could be worthless down the road and so if you elect to take equity, there's some probability that it will be worthless. And they probably need to be educated as to what that probability is historically so that people don't have unrealistic expectations of it. So the education piece has to be really important.

One aside, and I just want to add this. We did something at Cowen this year that -- where we granted everyone in the company equity. It's something -- and we're public but it's something we hadn't really focused on doing before, in part because, honestly, the proxy advisory services ding us every year on our say on pay because they think we give away too much stock. It's the craziest thing I've seen but it -- we basically get voted against on say on pay all the time because our stock compensation plan -- so much of our compensation is in stock.

But -- so we've got to rationalize this a little bit as these companies think about going public, that the proxy governance rules about how much stock you use to compensate employees, like that has to change too

otherwise you're going to have a bunch of public companies that have problems with getting say on pay done. And I think the SEC -- as these companies move from private to public has to have some oversight and some input on the say on pay rules for proxy.

But that aside, we did give everybody in the company stock, what we found is we had a lot of, even in our company believe it or not, a lot of financial literacy, so we're busy opening up brokerage accounts for people that didn't have brokerage accounts. I know everybody thinks that everybody on Wall Street must have a brokerage account, but the vast majority of our workers do not have brokerage accounts. And so the feedback that I've gotten as a CO, because we did it on top of compensation, we told everybody in advance that you're getting shares and then we communicated compensation separate so it was clearly in addition. The feedback that we got was overwhelming.

So the demand for people to be able to participate in the equity of the place where they work is 100 percent there and we are now going to be using that as a way to teach financial literacy and onboard people with Charles Schwab accounts so that they can become much more engaged. And having a conversation about why what they're doing at our company matters in

terms of the stock price and in terms of earnings and a bunch of other things that I thought we were talking about but I'm not sure that the vast majority of the company was really listening because they didn't own any shares.

And so I don't want to get lost. We could get lost in all the rules associate with this. This is absolutely critical to bridging the cultural divides, the social divides, even in a company like Cowen that everyone thinks is super sophisticated, what we're doing is turning inward and saying, “How can we be more socially equitable? How can we be more inclusive?” And we're benefiting from that in a way that I just hadn't -- just as a leader.

So I go back to the thing, it's leaders of companies should recognize that there are -- it's the right thing to do with your heart because it's the right thing to do but it's also a really good thing to do for building morale and building engagement. So anything we can do at the SEC to foster that is going to be really critical to enabling companies to build -- using corporate America, using companies to bridge the gap that we have in our country for sure.

So I just wanted to get that on the record and say that we're having a personal experience and it would be really great if we could figure this out.

MS. GARRETT: Okay. Thank you, Jeff.

And Sara, I see you have a question. I'm just going to make a quick comment real quick just to follow on Jeff's point.

So, Jeff, you mentioned that this was an equitable way for people in your company to all get to participate. I will just point out we're talking a lot about how we wouldn't want gig workers to get, you know, equity instead of compensation, cash compensation, but at this point in time under the 701 rules, gig workers aren't allowed to get any type of compensatory equity because they're not considered advisors or consultants so they're not able to participate, you know, at all.

So I think -- I think, personally, that the SEC, as Brian pointed out, is taking kind of a leading role in allowing these employees to be able to have equity in companies, which I think is beneficial to a lot of people. Now, whether that should be, you know, in addition to their cash compensation, I think it should be instead of, you know, an alternative to cash compensation. But I do just want to point out that under the current security rules they are not considered advisors or consultants and so therefore they would be prohibited from getting any types of options or

restricted units without this proposal going into effect.

Sara?

MS. HANKS: Yeah, actually to build on what you just said, Carla. I mean that there -- since 701 is not an option at the moment in those circumstances, we do see consultant-type people being compensated using Reg CF and I think that one of the things, I'd love to hear what Julie or Sebastian think, that there's anything in the Reg that says you can't do this. But I would think with Reg CF going up to $5 million and the fact that there are so few restrictions on who and what and how and how you price, I think we will see more people using Reg CF as a compensatory mechanism providing that there is an intermediary willing to host the offerings.

Because, obviously, if there's no cash changing hands there's no commission for them to make, but if they were to charge a fixed fee. Now, we do see Reg CF being used in experimental ways, shall we say, specifically giving people who are influencers better prices for the securities which, of course, raises Section 17(b) issues. But still, we see it being used in sort of free-ranging ways and I think CF is going to be an alternative for many companies to 701.

Sebastian? Julie? Wrong?

MR. GOMEZ: Sara, I hadn't thought about that question and I had not looked at the rules with an eye to whether it's something that is or is not permitted. But what I would like to say is go back to a point that Anne brought up earlier which is when Congress was assigning the right crowdfunding framework, I think it's pretty clear that Congress was not thinking of employees or gig workers in the context of that exemption. And I think probably it's not something that the Commission might have been thinking as the Commission was thinking about what's the balance of disclosure versus the limits that it will provide. So I think part of what, to me, makes me think about it is whether that's the intended tool for that and if so, are all the appropriate protections there for both sides, the companies and the investors, or in this case the employees.

MS. HANKS: From my own life as a former staffer I've had those conversations, specifically with respect to Reg S where at some point I've said, “That's not what it was for,” and people in large law firms were like, “Yeah, but you didn't prohibit it so we're using it for it.” So just heads up, I think that, you know, that there is an option there and if there needs to be some kind of guidance, that would be a good thing.

MS. GARRETT: Jason, did you --

MR. SOLOMON: Sorry, I'm not on mute because I'm eating, but Sara, you are 100 percent right. Like 100 percent right. And the Commission should think about guidance, prophylactically maybe, if that starts to happen because I saw the Reg S abuses happen and they were egregious and -- until the SEC put out guidance and then they stopped. But that's -- oftentimes there's a bunch of stuff that happens in the intervening period between the time the SEC gets around it and people get hurt.

And so I just think it's important. If we generally think that that could potentially happen, I think the SEC should be working on guidance about the use of Reg CF as an alternative to 701 and try to get out there and guide people to do the right thing before it starts to happen and then we got to react to it anyway.

MS. GARRETT: Thanks, Jeff.

Jason?

MR. SEATS: Which comment is the one that I -- that you want me to say?

MS. GARRETT: Well, maybe -- or I can have Sapna jump in. There was a -- looked like you both have some thoughts on this issue. It might be nice just to share them on the record.

MS. MEHTA: I'll just let -- I mean I'll let Jason continue. And I know this was not proposed but I think it just came up in conversation on the call. But just, you know, I think you're opening a huge can of worms if you allow employees to pick what form of compensation, of income they receive, whether it's in cash or, you know, equity. I think the financials of a company only offer so much insight into how they're going to do it. It's essentially a gamble. There are so many other factors that will determine the outcome of that equity --

MS. KRAUSKOPT: We've lost you. I think you've gone mute.

MR. SEATS: Oh, you're back.

MS. MEHTA: Okay. I didn't think I went anywhere.

MS. KRAUSKOPT: Well, we couldn't hear you but, you know, let me just point out that the proposal for gig workers would not let them make a choice and it would cap what they would get in equity at no more than 15 percent of the value of their services in the year. And furthermore, under 701 the securities would be restricted as to transfer so we would not be seeing a situation develop where, you know, you're not getting

enough cash, so you have to sell your securities to put bread on the table. You know, we don't want that to happen either to the gig workers and we don't want that to happen in making this proposal, if adopted, some kind of an -- on a registered public offering for capital raising.

We did have a history of S-8 abuses back in the 90's after it was opened up for consultants and advisors. And in 1999 we had to revise the rule to narrow and foreclose that possibility. So points about the SEC providing guidance to prevent issues, to prevent trouble from happening before it happens are good suggestions.

MR. SEATS: Yeah, I don't know that I had, Carla, that I really have a whole lot to add. I mean I -- to me, some of the really great points that were made from Kesha and Jeff on balancing the protections from -- giving wealth-generating access to people that typically haven't had that, right? And so I think the protections piece is super important but what you don't want to do is you don't want to protect people from wealth-generation, like you want to protect them from abuse, right?

And so I think the key is education and so I really -- I just want to underscore that. And I really

like Jeff's point of trying to ensure that the equity piece is something that's layered on top of cash compensation. Which I think the attempt here is to try to do that with that 15 percent restriction, you know, but you don't want to be displacing cash compensation because this stuff is highly illiquid, very long-dated, and also, I guess maybe one point I made in the comment thread is it's also not diversified.

And just the, you know, it's a lot of eggs in one basket to have your source of income tied to your equity wealth-generation as well and so that's, you know, it is different than a retirement account that's being invested in something that's diversified and stable. And so -- but on the other hand, like again, you don't want to protect someone from actually getting an upside, right? Like -- so I think that's the balance.

So I think education is a super-big component of this and also maybe I would underscore the point that Jeff made which is in what you might view as sophisticated companies with lots of, you know, knowledgeable workers, the -- you'd be shocked at how few people really understand how even just stock options work in startups. And I think there's -- I think that there's probably some work to do there and I don't how

we do that but that's important work.

MS. GARRETT: Jason, I'll just go ahead and agree with you. Anne was pointing out, for instance, that the securities would be non-transferrable and have transfer restrictions on them, but that's a word that we all understand on this call, but I would imagine that's not a concept that a lot of the gig workers would understand without education. So I believe education is also very important, though I also believe that, you know, protecting people so much from where there is no potential of an upside wasn't -- isn't our goal either.

Do other people have comments that they'd like to make on this? We're running up against 2:30.

MR. YADLEY: Carla, I think this really is important and I applaud the SEC in taking the lead and tackling these issues that Jeff appropriately characterized as cultural and social. I think the guardrails on the limits of the amount of stock issuance are helpful. I don't really have a view yet as to whether those are the right caps but conceptually it makes sense.

And what Sapna was saying, optionality is a critical point, not just for, you know, are we being too paternalistic or are we being exclusionary but making this an investment decision raises a number of issues, not the least of which are potential liability and disclosure. And one of the main reasons that companies like being not public, D&O insurance was mentioned this morning, is they don't want to get sued and it's easier to get sued as a public company. And the other thing is, and this is already part of the Rule 701 regimen is information. Another advantage of not being public is you have more control over information that you consider confidential and it's your information, so you get to decide. If you are issuing securities as an investment, then there's a legal definition there.

So the integration of all of these is very complex, but like a lot of issues, we won't get anywhere if we don't tackle them and this is an area where I'm glad the SEC is being proactive.

MS. KRAUSKOPT: One thing I would want to point out, you talk about information, the technical release which I described first, does have proposals that relate to modifying the disclosure requirements as they relate to larger 701 offerings.

Those of you who are particularly interested in the gig economy release, they want to look at the technical release and consider whether the disclosure proposals articulated there which would be permanent rules, they would not be part of any sort of temporary

rule, they are -- would be built into 701. Whether they make sense for gig employees given that they would apply in that context as well as in the context of the persons who currently are eligible.

MS. GARRETT: Thank you, Anne.

Okay. If nobody else has any further comments, I want to thank the group today for everyone's participation and for tackling some very tough policy and legal issues. At this point we do not have dates yet for our committee meetings for the rest of 2021, but we plan to get those dates on people's calendars soon. And I hope everybody stays well and stays safe and thank you for participating.

And, therefore, I hereby adjourn the meeting.

(Whereupon, at 2:33 p.m., the meeting was adjourned.)

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PROOFREADER'S CERTIFICATE

In The Matter of: SMALL BUSINESS CAPITAL FORMATION ADVISORY COMMITTEE

DATE: Friday, January 29, 2021

LOCATION: Washington, D.C.

This is to certify that I, Christine Boyce, (the undersigned), do hereby certify that the foregoing transcript is a complete, true and accurate transcription of all matters contained on the recorded proceedings of the meeting.

______________________ 2-5-2021

(Proofreader's Name)

REPORTER'S CERTIFICATE

I, Kevin Carr, reporter, hereby certify that the foregoing transcript of 151 pages is a complete, true and accurate transcript of the meeting indicated, held on 1-29-21 at Washington, D.C. in the matter of: SMALL BUSINESS CAPITAL FORMATION ADVISORY COMMITTEE.

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

2-5-2021

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