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SMALL BUSINESS CAPITAL FORMATION
ADVISORY COMMITTEE

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U.S. Securities and Exchange Commission
100 F Street, N.E., Washington, D.C.

PARTICIPANTS:

Commissioners of the Securities and Exchange Commission
GARY GENSLER, SEC Chairman
JAIME LIZARRAGA, SEC Commissioner
MARK T. UYEDA, SEC Commissioner
CAROLINE CRENSHAW, SEC Commissioner
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JASON SEATS
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MARC OORLOFF SHARMA
HANK TORBERT
SUE WASHER

SPEAKERS:
RYAN FEIT, CEO and Co-Founder, SeedInvest
JOAN ADLER, Partner, Ellenoff Grossman & Schole, LLP

C O N T E N T S

P R O C E E D I N G S

INTRODUCTION

MS. GARRETT: Good morning, and welcome to today's meeting of the SEC's Small Business Capital Formation Advisory Committee. It is good to see all of you, and we appreciate members of the public who are tuned in to watch the meeting being broadcast on sec.gov. I hereby call the meeting to order. Julie, do we have a quorum?

MS. DAVIS: We do.

MS. GARRETT: Thanks. Thank you to the members of the Committee who continue to join these meetings virtually. I look forward to the day when we can meet in person again but appreciate everyone's commitment to this Committee. And I also want to thank the staff of the Office of the Advocate for Small Business Capital Formation all who play and integral role in having these meetings come together.

And finally, I'd like to extend a special thank you to the Chair and the Commissioners for attending today's meeting. In particular, we wish to extend a warm welcome to the two newest commissioners, Commissioner Mark Uyeda and Commissioner Jaime Lizarraga. Congratulations on your appointments, and we very much look forward to working with you. I hope I speak for all members when I say that it's a pleasure to serve on this committee, and we all care deeply for the SEC's important mission.

For our agenda today, we'll start with members sharing their firsthand observations and perspectives on the capital-raising landscape for small businesses. Since the onset of the pandemic we have periodically had members share updates on what they are seeing in the market. For our second agenda item, the Committee will discuss secondary liquidity challenges for investors in small and emerging businesses.

In planning this meeting, we initially thought that we would have a morning session focused on secondary liquidity issues for Reg A and Reg Crowdfunding companies and an afternoon session that focused on secondary liquidity for smaller public companies, but as we thought through the issues more it seemed that the two issues flowed together and were similar in their respects that it made sense to have just one longer session. Therefore, we will just have one session today until 1 p.m. without a lunch break.

We've lined up guest speakers to present on the topics, and I look forward to the Committee engaging in discussions with them and with each other. Before we turn to our agenda items we are pleased to first recognize the Chair and Commissioners for opening remarks. Chair Gensler, thank you for joining us today.

INTRODUCTORY REMARKS

CHAIRMAN GENSLER: Thanks so much, Carla, and all the committee members. And as is customary I'd like to note that my views are my own, and I'm not speaking on behalf of the Commission or the SEC staff. It's good to be with you today. It's also good, as Carla said, to be with my two new -- newest, I should say, colleagues on the Commission, Commissioner Mark Uyeda and Commissioner Jaime Lizarraga. Last week Jaime and Mark introduced themselves to the SEC staff, was sworn in a little while before that. I was pleased for the opportunity to learn more alongside the staff about both commissioner's professional achievements as well as their rich personal stories.

Jaime and Mark each come from families that started -- yes, families that started their own small businesses. So I look forward to varying sides on the Commission, including as it relates to the important work of this Committee and the issues about small businesses. I hope you can all join me in welcoming Jaime and Mark to the Commission.

I also look forward to learning about the Committee's discussions on today's two agenda items.

First, I'm interested to learn what the Committee sees on the horizon for small business capital formation. I hope that you'll discuss I would say both the longer-term trends about rapidly changing technology and the present day considerations as it relates to the economy.

With regard to technology, I continue to believe that we're living in truly transformational times. Many financial technologies are being used both as startups by so called fintech startups and by financial incumbents or even big tech incumbents in offering new ways for small businesses to borrow and raise money. How is this affecting the availability of capital? Should it change at all how the SEC is overseeing the markets and, if so, how might it change how we're overseeing the markets? So that's the longer term but very with transformational trend about technology and raising capital.

But also as it relates to the current economy we're living in uncertain economic times whether that be from the ongoing war in Ukraine and commodity price surges and the like to the pandemic itself to central banks around the globe transitioning from an accommodating to a tightening policy stance. How is that affecting small businesses? How is that affecting how small businesses raise money in the capital markets?

I look forward as well to the Committee's discussion on secondary market liquidity for small businesses whether it's Regulation A, Regulation Crowdfunding or smaller public companies, and I'd be interested to learn about the Committee's thinking on these matters as relates to promoting investor protection facilitating capital formation.

With that I'd like to turn things over to the Committee. My thanks to our two guest speakers who have joined us to discuss the matters. My thanks to the Committee members for their time and service. I hope today is productive.

MS. GARRETT: Thank you, Chair Gensler. Commissioner Peirce.

COMMISSIONER CRENSHAW: Commissioner Peirce, I think you're muted.

MS. GARRETT: Should we go to Commissioner Crenshaw until we figure out Commissioner Peirce's audio?

COMMISSIONER CRENSHAW: I'm happy to, but Commissioner Peirce, do you just want to dial in on your phone? No. Okay.

MS. GARRETT: Commissioner Crenshaw?

COMMISSIONER CRENSHAW: Sure. Good morning, everyone. It's good to be here, and as always these advisory committees are so important in bringing together multiple perspectives to help the Agency think through some of the most difficult policy issues that we face, issues that impact investors and markets every single day.

And as you know, it's hard work that involves tradeoffs and a careful balance of the costs and benefits and low-hanging fruit and really the easy layups seem harder and harder to come by these days. So all of the issues that we face are challenging ones. So thank you to the members of the Small Business Capital Formation Advisory Committee, all of you for your time, your dedication and your service, and I am looking forward to today's presentations and discussions about secondary market liquidity in Reg A and Reg Crowdfunding deals.

One of the first questions that comes to mind for me are whether the disclosures investors and particularly nonaccredited investors receive before committing capital, and are these disclosures adequately helping them weigh the risks upfront, including informing them of the likely exit opportunities and the timelines? And are the required intermediary disclosures under Reg Crowdfunding working as intended, or are there areas for improvement here?

Something I'm often thinking about is investor testing and whether that could be a meaningful tool here as it could be with some of our disclosures in other areas that really have high direct participation readership. So I'd be interested in your thoughts on that.

And in addition to disclosures a couple of others questions have come up for me when I'm thinking about this space including one -- there's a recent staff study from 2020, and it got me thinking about a couple of things. So the 2020 study noted that 75 percent of Reg A offerings had no secondary market with 21.7 percent trading in OTC markets and 3.2 percent of Reg A issuers being exchange listed.

And so I'm interested to know what's happened with the 75 percent of Reg A offerings that had no secondary market? Were there eventually exits, and was there use of green markets, and what is or was the success rate of those issuers in this subset? And what were the implications for future raises that those issuers may need?

In addition to that, what did investors understand as they were looking into these investment opportunities? And so for me, generally speaking, more data is often helpful for making informed policy decisions, and the 2020 staff study provides important insights into Reg A and Reg D offerings, but it was conducted before the most recent amendments to the exempt offering framework, and it does have some limitations. It's certainly limited because the data that we have in this space is a bit limited particularly in the Reg D space.

So I would urge the Advisory Committee to consider whether other data would be useful to you all as you're considering these questions and to other policy makers in this space as we seek to improve investor protections and to promote capital formation for small businesses. Further study into the effects of the recent changes and a study that includes Regulation Crowdfunding and other exempt offerings may prove instrumental in any future reforms that we're considering, and I'm sure that many great ideas to address the practicalities and the hurdles in secondary market liquidity will be identified here today, and so I am looking forward to it and to the larger discussion. Again thank you all for your time, your service and your expertise.

MS. GARRETT: Thank you, Commissioner Crenshaw. I apologize. I had myself on mute. Commissioner Peirce, let's see if we can hear you.

COMMISSIONER PEIRCE: Can you hear me?

MS. GARRETT: We can.

COMMISSIONER PEIRCE: All right. Well, maybe I was muted by the system so that I could second Commissioner Crenshaw's call for good data. Anyway, I do want to thank everyone and am glad to have both our Committee members here today and our panel as well, and I'm pleased that we'll be talking about a critically important topic for small businesses. There are many Americans who would like to invest in mainly secondary market liquidity.

Pursuant to mandates under the now decade's old Jobs Act the Commission developed rules to broaden the ability for smaller companies to sell their shares directly to retail investors. Reg Crowdfunding and Reg A+ has allowed individuals to invest in companies at a much earlier stage of growth than typically is possible through a traditional IPO.

Investor protection is the top consideration when retail investors participate in these kinds of offerings, but as originally drafted Reg Crowdfunding and Reg A+ got the investor protection investor choice capital formation balance wrong. Accordingly, under Chair Jay Clayton's leadership during the pandemic certain crowdfunding rules were adjusted temporarily, and in 2020 the SEC made permanent changes to both Reg Crowdfunding and Reg A+ as part of a broader package of reform.

While the amendments were helpful we can do more. One area for further reform is the one on today's agenda. Secondary market liquidity marries capital formation and investor protection consideration. Issuer's ability to raise capital turns in part on whether purchasers of their securities will enjoy strong secondary market liquidity. We've heard in the case of small cap issuers of publicly-traded securities that secondary market liquidity is key to their ability to hire and retain employees as well as to raise additional capital.

Again, I don't think a liquid secondary market benefits investors who want to realize gains from successful investments or otherwise move their money into new areas. So again I don't think there's a tension between capital formation and investor protection. Increasing secondary market liquidity can protect retail investors.

As the Commission staff noted in a recent report most Reg A issuers do not have a liquid secondary market for their securities which can make it difficult for investors to sell their investment quickly without a loss of value, and the same is true for Reg Crowdfunding issuers. Today this Committee is shining the spotlight on secondary market liquidity and shares sold through these types of offerings as well as publicly-traded companies.

Spotlighting these issues is a good start, but we could benefit from the searchlight to identify specific ways in which we can improve secondary market liquidity. I look forward to hearing from committee members and panelists on any issues you think are important in this regard. I do have several specific questions.

First, what opportunities do investors who purchase shares through a crowdfunded or Reg A+ offering have to sell the shares they hold? How do these differ from opportunities available to investors who purchase shares through other types of private offerings? How are companies that have issued shares under Reg Crowdfunding or a Reg A+ offering affected by limited secondary market liquidity? How are investors that have purchased shared under Reg Crowdfunding or Reg A+ offering affected by limited secondary market liquidity?

The 2020 Small Business Forum recommended state preemption for secondary transactions for shared issued under Reg A and Reg Crowdfunding. Do you agree with that recommendation? What regulatory provisions other than the lack of Blue Sky preemption has hindered the uptake of Reg A+ and Reg Crowdfunding? Can new technologies such as Blockchain, smart contracts or better auction technologies habilitate secondary market trading? If so, are rule changes necessary to allow people to put these new technologies to work for this purpose?

Thank you, and I look forward to the discussion.

MS. GARRETT: Thank you, Commissioner Peirce, and thank you for posing different questions for us today.

Commissioner Uyeda, welcome to the Committee, and we look forward to working with you.

COMMISSIONER UYEDA: Well, thank you, Carla. Good morning, and welcome to each of you. It's a pleasure to participate for the first time with this committee as a commissioner, but as a longtime SEC staff member it's great to see some familiar faces today some going back to the earlier Advisory Committee on Small Emerging Companies. Sara, Greg, Catherine, I remember you. There may be others from back in the time. So good to see you again, but I also enjoy seeing the new faces, and I look forward to working with you in the future.

During my confirmation hearing, I described working with my grandfather on a small produce delivery route in Southern California. I saw firsthand the challenges and obstacles with operating a small business including the need to raise capital. This experience impacts the prism through which I look at small businesses. Small business owners work to grow and prosper every day, and they require a stable and predictable regulatory framework for capital formation.

At my last assignment as a detailee to the Senate Banking Committee I had the opportunity to review and discuss your recommendations on small business capital formation with my colleagues on the Hill. I can assure you your work provides helpful ideas for capital formation that receive attention from policymakers.

One of the things that Commissioner Crenshaw mentioned which I fully agree with us our ability to engage in investor testing that was authorized in Section 912 of the Dodd Frank Act. I think it's an underutilized tool and that there is much to be gained from robust testing of the disclosures made available to investors. I think there are a lot of other ideas, though, that can be put forth to policymakers.

With respect to your Committee, I know that some of your recommendations have been included in the draft Jobs 4.0 Act legislation currently being circulated for discussion in Congress. For example, your recommendation on qualifying venture capital funds influence, Section 202 of Jobs 4.0 while your accredited investor recommendation is reflected in Section 306. Commissioner Peirce and Commissioner Crenshaw both also discussed about the need for liquidity of Reg A+ offerings in secondary transactions.

This is also an issue that at least Jobs 4.0 tries to address with respect to preempting state securities regulation with respect to issuers that are current in their Reg A+ reporting, but I realize there are potential drawbacks with that, too.

Indeed NASAA, the North American Securities Administrators Association, testified at a Senate hearing last week about those concerns. So I look forward to continued debate as to how we might improve liquidity for Reg A+ offerings. Your advice and recommendations are particularly relevant for financial regulators more broadly whether it's your recommendation on finders or your recommendation on SPACs as to whether SPACs remain a viable path for companies to pursue access to the public markets. These issues and others impacting small businesses are of great interest to me personally and to market participants generally.

So to close, I want to commend each member of the Committee for the service you render. You play an important role in identifying regulatory obstacles to capital formation. Hopefully, we will soon be able to convene and meet in person, and I look forward to that day. Thank you.

MS. GARRETT: Thank you, Commissioner Uyeda, and welcome once again to the Committee or to the -- sorry, at the Commission. Commissioner Lizarraga.

COMMISSIONER LIZARRAGA: Good morning, Chair Gensler, fellow Commissioners, Carla. Thank you for the welcome, and thank you to the rest of the Committee for your time and input today. It is a pleasure to address and SEC Advisory Committee for the first time, and our topic is profoundly important to small business capital formation. I should note here that as always the remarks I deliver today are my own and do not represent the views of the Commission or its staff.

In preparing for today's events, I revisited the legislative history of the statute that established the SEC's Office of the Advocate for Small Business Capital Formation and its Advisory Committee. What stood out to me is how smoothly the legislation vote by voice vote in the House and by unanimous consent in the

Senate with no amendments. This swift enactment demonstrates the strong support in Congress for this office and for this Committee's essential role in advocating for small business capital formation and small business investors.

As members of this committee, you have a unique opportunity to shape the regulatory dialogue. It's a commitment that I know you take seriously and that adds distinct value to the SEC's capital formation mission. Central to the Office of Statutory Mandate is reporting to Congress on the most serious issues encountered by small businesses and small business investors. A few key findings from the office's latest annual report bear mention here.

On the plus side, the representation of women is steadily increasing on corporate boards and in the boards of venture-backed private companies. I'm also encouraged to see growing recognition among investors about the value of diversity and inclusion. However, the annual report also highlights significant concerns. With respect to capital formation more broadly, mature and later-stage businesses are seeing limited opportunities to access venture capital outside of existing personal and professional networks.

In addition, there are persistent challenges unique to minority women-owned businesses. Capital raising by women-owned businesses pales in comparison to the proportion raised by men-owned businesses. Many underrepresented entrepreneurs confront additional barriers due to the well cap. A large percentage of LGBTQ plus small business owners cite raising capital as their greatest business challenge.

The share of minority entrepreneurs seeking angel capital in 2020 dropped 4 percentage points related to 2019 another likely indicator of the disproportionate impact of the COVID-19 pandemic on minority entrepreneurs.

The notable lack of significant progress in these key areas illustrates the need for exploring new and innovative regulatory solutions that can address existing disparities. Proposals to adjust regulation in traditional ways must be evaluated against whether they truly level the playing field for all market participants. Meaningfully addressing the unique challenges that women and minority-owned businesses face is critical to fulfilling the SEC's capital formation.

I would note, by the way, that the phrase “unique challenges” comes directly from the authorizing statute and is additive to other challenges small businesses face. I had a front seat view of some of these challenges as the son of immigrant small business owners who ran a Mexican food business out of our home. The barriers to their businesses' growth are common to many immigrant families -- language difficulties, a financial system they perceive as unapproachable or out of touch with their needs and deeply ingrained cultural practices surrounding the search for growth capital.

This is on top of all the usual capital-raising challenges that small business owners face some of which are also highlighted in the annual report. The Advisory Committee can be instrumental in arriving at viable solutions to these unique challenges. The statute was written to ensure that the voices of officers and directors of women or minority-owned businesses are not only heard but represented on the Committee. Your role is vital to ensuring that millions of small businesses across America can have the best possible opportunity to grow and succeed.

I urge the Committee to keep these unique challenges at the forefront as it considers how best to address liquidity in the secondary market, markets for private offering. Thank you for your valuable contributions, and I look forward to today's discussion.

MS. GARRETT: Thank you, Commissioner Lizarraga. We are excited to be working with you.

Welcome. And thank you to the Chair and the Commissioners for attending today. It's always a pleasure to see everybody.

Now we're going to turn to our first agenda item. With so much going on in the broader national economy, the time seems right for being the first to share observations from our various sectors with respect to small business capital formation. We will go around the proverbial room and hear from committee members. Please note that the SEC staff will put in the chat box the speaker order, and each member can take up to three minutes to share your perspective.

This time we are going to start in reverse alphabetical order, and that means that Greg will have the honor of going first. Greg. You're on mute, Greg.

COMMITTEE MEMBERS' OUTLOOK: WHAT'S ON THE HORIZON FOR SMALL BUSINESS CAPITAL FORMATION

MR. YADLEY: Sorry about that. I too wish we were in the same room. Since we're going in reverse order I will note that I am not in the same place as Youngro, but we have reverse images in our backgrounds, so we're in the mountains somewhere. I'm actually at my desk.

There's a great deal of capital out there. There has been, and COVID and the economy haven't really changed that. Deals continue to get done. They are taking a little bit longer in part I think because the atmosphere is less frenzied as there's more caution certainly where institutional capital is part of a deal. Underwriting is taking longer. Due diligence is being more diligently pursued, and at the lower end of the market angels continue to provide meaningful capital, but it's still tough for startups.

In thinking about what we're doing at our firm and what we're seeing, I have to say it's been a mixed bag. I'm in Florida entertainment. The space is wide here, and I've seen both sides of it. One of our film clients which has been successful got lukewarm support for a private placement and has decided to defer that. On the other hand, a capital raise in connection with a DSPAC transaction for an attractions client presented no problem. And, in fact, much of the capital-raising that we've seen recently has been in connection with M&A activity. M&A has been very strong nationally, certainly here and particularly in real estate and related development such as hospitality.

I think reflective of other areas of the country tech and healthcare have been the biggest sectors where local deals have gotten done. We had a telehealth company in St. Petersburg close to $5 million

Series A round a couple weeks ago, provides access to pharmacists via its telehealth platform. A couple of SAS companies, one community focused have gotten funding.

A kidney population health management company completed a $35 million round, and a software company that supports and manages customer experience did a small million dollar round including $600,000 from Tampa Bay Ventures, a local funding source. And we have a new marquee company, a cybersecurity firm ReliaQuest which hit the billion dollar mark at the end of the year and is how the name sponsor of what used to be the Outback Bowl played on New Year's day here in Tampa.

Other sectors have gotten funding recently. A private jet company even post-COVID completed an almost $10 million Series A round. A natural food brand company in the Bay Area did some $10 million Series D round, payroll, fintech. But a lot of these have been funded from outside of Florida. Particularly in the healthcare space there have been companies from the Midwest and New Jersey area that are industry players, major brands sort of trying to expand their footprint through smaller companies.

I think looking forward that over the next 6 to 12 months the market for small business capital will be choppy. Private funds will continue to provide support. I mentioned Tampa Bay Ventures. The funding that I referenced was the seventh investment for the fund which makes small investments. They've put $3 million plus out there now, but they're able to act pretty quickly. We also saw the creation earlier this year of a $13 million fund new technology focusing on companies with less than a $50 million valuation post investment.

So I think people still want to do deals. There's money out there, but the barriers that several of the commissioners have mentioned remain there for women and minority-owned businesses, but people are paying attention, and I am cautiously optimistic that we will continue to get deals done in the small business and lower middle market. Thanks, Carla.

MS. GARRETT: Thank you very much, Greg. Sue.

MS. WASHER: Yes. Thank you for the time to speak today to the commissioners and to this committee. My world is a little bit different potentially and specialized than others. I run a biotech company. We went public several years ago through the traditional IPO method and raising capital on follow-on markets.

The biotech sector is a unique sector as I'm sure many of you are aware. The amount of financing that it takes to bring a new human therapeutic or even a diagnostic or a medical device to market is hundreds and hundreds of millions of dollars. So biotech companies are heavily reliant on public markets to finance themselves through to a point where they have a approved product, and the last year and a half has been exceptionally challenging for biotech companies.

Last year the biotech index went down 37 percent. This year it's down already almost another 30 percent, and fundraising in the biotech sector is exceptionally challenging. Year-to-date there's only been 55 total deals, public deals, in biotech compared to 232 by this time last year, and half of those 55 deals are trading under their issue price.

There are literally hundreds of biotech companies trading below their cash-on-hand which shows the discouragement in the investment community around biotech companies. There's only been nine IPOs so far this year, and half of those are trading below their issue price, and there's only seven IPOs on file.

So these are very, very low numbers in the biotech industry, and honestly I'm in this sector, but we really believe that this sector is the life blood of the American economy and certainly the life blood of providing very high-quality needed medicines to our population. And it's very concerning to us the level of difficulty that companies are having to attract investment.

And just to kind of segue a little bit and foreshadow into our next discussion some of this does has to do with the secondary markets and liquidity and investors seeing such a depression in overall stock indices and an uncertainty about the future that the day-to-day trading volume is low. So then even for investors that really want to get into a name and want to fund a name they become very concerned about future liquidity for the company, and with so many companies trading at cash or below cash there's also a cap on how much money they can raise.

Biotech companies are used to raising $20- $50- $100 million at a time, but if your market cap is down below 200 million you can't raise that amount of money, and so the number of companies that have less than two years or even less than one year of cash-on-hand is quite alarming. So it is very challenging. The Biotech Industry Organization, the Alliance for Regenerative Medicine and other trade association groups are trying to work very hard on this and figure a way to help companies.

One of the most common outcomes in these kind of situations is that there starts to be a lot of strategic interest from the very large pharma and biotech companies. That hasn't started to happen yet, and there's been some level of concern around some of the comments from the FTC about their concern about mergers and acquisitions as being limiting to competition. And so that is very concerning to our sector because that is generally the alternative to funding very important medicines when the equity markets become more challenging.

So there's a lot going on in our sector. We're all watching it carefully and very concerned about capital availability. And I know that many times biotech companies are considered to be very big. They look very big many times because of their market caps, but they're generally small companies focused on one or two lifesaving medicines, and their market cap is really not a function of revenue. They don't have revenue for many, many years.

So those are my concerns and observations for my specific sector of small cap biotech companies.

MS. GARRETT: Thank you, Sue. I appreciate those comments, and hopefully we can address some of those later on in the meeting. Hank.

MR. TORBERT: Hi. Good morning, everybody.

My name is Hank Torbert. I'm the president and owner of Alta Max which is a manufacturing business focused on the munitions packaging space. I'd say several factors impact the valuations of businesses in my space, which is a middle market space, as well as the access to capital. Over the last year and a half we've had major disruption in our supply chain as well as significant labor shortages all of which results in slower revenues, declining revenues and, in fact, in many instances it's gotten so bad for some operators that they're simply selling their businesses or pulling out of certain sectors.

All of this results in a tightening of capital available to companies in this space, quite frankly, and as well with the increased interest rates that also makes it very difficult for smaller-sized businesses to operate and to function. So unless you are well capitalized, and luckily we are, many businesses are having significant problems right now.

And then lastly, for those of you who are the children and grandchildren of entrepreneurs who joined this committee, I want to say thank you very much and glad we have that in common because I'm also the three generation entrepreneur as well. Thank you.

MS. GARRETT: Thank you very much, Hank. We have next Marc.

MR. SHARMA: Thank you, Carla, and good morning everyone. I’m Mark Sharma. I'm the representative of the SEC's Office of the Investor Advocate on this Committee. First, I would reiterate and agree with the comments made by our chairman and commissioners, but I would also say that we in the Office of the Investor Advocate are extremely idea in the views that you have to share.

So to all the members of the Committee, I would say please do reach out and engage with the Office of the Investor Advocate to the extent you wish to share your concerns, share the issues you're facing with us to the extent that we can engage in this conversation, to the extent that we can be helpful.

One of the things I miss about us meeting in person is our lunchtime members offline where we could speak candidly with each other and share our views and have a very helpful back and forth, and I hope to regain those days in the near future. But in the meantime, feel free to engage with our office offline and share your concerns, share your views with us because too often my office is hearing from large institutions, and there is a lacuna in terms of the views that I would be hearing from you. So please do engage with our office to the extent we can be helpful.

And also feel free to engage with your sister committee, the SEC's Investor Advisory Committee. I know Catherine Mott is friendly with Christopher Mirabile who chairs the Investor Advisory Committee. So it would great to get those dialogue going between the two committees because there are a lot of common issues that the committees share. And I will end by saying there is an Investor Advisory Committee coming up on September 21st if you're interested.

There will be a lot of hot topics discussed, a lot of recommendations on hot topics that I believe are of interest to you. I cannot disclose what they are at this time, but if you're able to join the September 21st meeting, please do so. And with that, I hand it back to you, Carla. Thank you.

MS. GARRETT: Thank you, Marc, and thank you for those different recommendations. Andrea.

MS. SEIDT: Thank you, Carla. Good to see everybody today. I'm going to keep my remarks brief because I want to reserve my time to share my thoughts on state preemption during Session 2. Probably no surprise to most of you. What I would say and I think one of the commissioners pointed this out is that NASAA recently testified before Senate Banking about investor threats in the past year, and what they highlighted were threats in cases coming out of crypto and digital assets and also sharing enforcement cases involvement private and exempt offerings.

In Melanie Lubin, who is NASAA president's, testimony, she shared some of the research that I do every year for an ALI Reg D conference. I joined Sebastian and Jennifer Sapalga from the Commission to share regulatory views and things that we're seeing in the private and exempt offering space, and I was able to compile over 120 state enforcement actions -- these are administrative actions -- involving exempt and private offerings in just 2021 alone. So if you want to learn about those cases, where they're coming from I think almost all the states in the country, I encourage you to go to NASAA's website and pull up Melanie's testimony because those cases are there.

The only other thing that I would add is that I also echo the commissioners' comments, several commissioners' comments that more data is needed to the extent we consider policy in this area. So thank you for your time. I'll reserve my minutes for Session 2. Thank you.

MS. GARRETT: Thank you, Andrea. Don't feel like you have to reserve your minutes for Session 2 because we know you're going to be speaking, and we're not going to limit you to three minutes on that I promise. So thank you. Jason.

MR. SEATS: Thanks, Carla. I'm Jason Seats, Chief Investment Officer at Techstars, and we're an early-stage venture investor investing -- I'm based in Texas, but we invest broadly across all places in the U.S. and also much investing outside of the U.S. My comments will be specifically in regards to venture-backed startups in terms of small business capital formation.

So in Q-2 the trend has been an overall decrease in the dollar volume of funding for venture-backed startups although still from an overall standpoint very high level of funding. And a way to think about this is we're maybe at 2020 levels or approaching those levels whereas 2021 was a record beating off the charts sort of level of capital flowing into this asset class.

The main driver, obviously, rate environment, compression of equity multiples in the public markets. In venture, that tends to start from -- that effect starts at the largest businesses, so the sort of pre-IPO growth stage companies and the funding environment there, and it takes time to work its way to the earliest stage of investing, seed stage investing, which is where we operate.

The venture market is seeing the biggest impact in growth stage valuations and dollar flow. Interestingly, the earliest stages in Q-2 are still seeing generally stable and even depending on how you look at it an increase in overall funding over Q-1 of this year so still taking a little while to sort of work its way through to the earliest stage.

So like most other venture investors we are spending a lot of time counseling our portfolio companies to be cautious about the current market and expectations and ability to raise money. There is a lot of, as we say, dry powder available. A lot of venture firms have raised money that is waiting to be deployed. It's uncertain if investing behaviors will change substantially from where they are now, but many are eager to call a market bottom at any point although there are plenty that have seen cycles before and think that we still have a more protracted reset ahead of us. You would probably put me in that camp.

But overall I would say that there is still a relatively high level of uncertainty about expectations of capital availability for venture-backed startups. Thank you, Carla.

MS. GARRETT: Thank you, Jason, and I appreciate your optimism. Catherine.

MS. MOTT: Thank you, Carla. I am going to talk a little bit about what I see and live in my footprint here in Pittsburgh. We serve venture-backed companies with two entities, an angel group and a venture fund -- and venture funds, I should say, and our footprint is primarily Pittsburgh through Chicago.

I will address that I continue to see a concern with the dearth of runway capital, and I define “runway capital” is the point between seed funding and profitable exit, so after seed funding. Seed funding has grown tremendously in the past 20 years. Great with crowdfunding and other resources, but unfortunately for the middle of the country we’re underserved, and underserved populations, I should say, also should be addressed here.

We have datapoints that show that 74 to 80 percent of VC dollars remain within the coastal regions. That's California, Boston, New York. In the flyover parts of the country, we have ecosystems supporting entrepreneurs who are launching competitive advantaged products and services, and unfortunately the capital required to support their growth remains on the coast.

And let me speak specifically about a lot of these companies. Plentiful top universities that are rich in intellectual property are in flyover parts of the country and have spun out this IP for some significant growth opportunities in tech and pharma and other areas. We all know also that creating and growing jobs locally contributes significantly to a healthy community, but we have to address the capital gap needs in order to serve these companies to grow adequately.

We need alternative structures to fund and support the growth of these young companies that are not located in a coastal region. We've discussed this in the past by addressing the 99 Investor and the 250 Investor Rule with either a larger cap of investors or even a mutual structure.

One of the things I've seen in my region is professionally managed angel groups are trying to attempt to serve this gap by launching funds, but the restriction of 250 with a $30 million cap does not move the needle. What I mean by this is in order to have a healthy venture capital fund you have to be able to spread your risk across 20 to 25 companies, and when a company -- and we say Series A is somewhere between 3- and 15 million or have between 5- and 20 million depending on where you're located. A small fund of 30 million can't deploy the capital required to get to 20 to 25 companies when companies at this point in time need us to make a $5- to $10 million investment.

So at a point where companies need this to advance angel funds haven't been able to even be able to move this enough to really critically serve the gap. So essentially this sector that I'm talking about deserves to be better served with runway capital, and we need to find alternative methods to do that. Thank you very much.

MS. GARRETT: Thank you very much, Catherine. Appreciate those thoughts. Sapna.

MS. MEHTA: Hello everyone. Nice to see you. Jason and Catherine, thank you for teeing me up perfectly with your background. Just for some background for those of you I don't know I'm associate general counsel at Revolution and general counsel of our two seed funds, the Rise of the Rest Funds. Like Catherine was saying we focus our attentions not on any one particular industry but rather on geography or, you know, anywhere outside of Silicon Valley, Boston and New York.

And so we are still deploying capital. In terms of some trends we have seen, we are seeing fewer SPACs although one of our companies just successfully DSPAC'd last week, so that was a great fiscal note, but we're not really seeing as much interest from our companies in the last six months or so. We are seeing -- at this stage, we invest in venture-backed seed stage companies, and we are still seeing quite a bit of activity although we're seeing a lot more top-up rounds rather than new priced rounds.

So a lot of companies are just opening up their last round just to have a little bit more runway. They're not quite sure what the next 6 to 12 months are going to bring, and so they're more focused on just hunkering down, focusing more on, like, business fundamentals rather than growth. I think we're definitely going to see some of those effects later on down the line.

We are seeing -- to Catherine's point, we think it's critical to have a robust bond economy in the rest of the country. A lot of these companies that we are seeing continue to get funding is because of some of the regional funds that are stepping up to take a little bit more of the round, and that's great. I just worry what's happening with the fund formation. There's always a lag, and so if there aren't going to be as many people investing in these regional funds then they won't have the money to then invest in these companies.

We haven't seen the effects quite yet, and so

I am interested -- I know it's not on the agenda today, but I know the House just passed a bill, the Deal Act, and they're addressing secondary sales so whereas earlier-stage investors and founders can sell their shares, and venture funds who qualify for the venture capital operating exemption can purchase those without hitting its 20 percent nonqualifying investment basket.

I know that the fund to funds piece was stripped from that bill much to my dismay. I've spoken about it before, and I think this goes hand-in-hand with what I'm talking about because if we don't have these robust regional funds that are getting funding from a lot of larger funds, coastal funds, then we are going to see some funding dry up I think in the rest of the country. I think that's all I have to say for now.

MS. GARRETT: Thank you very much, Sapna. Brian. Good to see you.

MR. LEVEY: Good to see you, Carla. Thank you. For those of you who don't know me, I'm Brian Levey, Chief Business Affairs and Legal officer at Upwork, which is a large talent marketplace for remote talent. Some observations. Upwork recently conducted a survey with over 400 hiring managers at small businesses. No surprise the great resignation is obviously impacting small businesses. Talent shortages, skills gaps, ability to quickly hire full-time employees persist as big issues especially in such a competitive hiring market.

We're also seeing that small businesses are increasingly comfortable working with independent remote talent or freelancers. Two-thirds of the businesses surveyed indicate that they lean on independent talent in some capacity. So in light of these observations on sort of the macro scale I do have one tangible suggestion as it relates to enhancing capital formation under Reg A.

Right now smaller businesses who want to sell shares in Tier 1 and 2 offerings under Reg A need to complete Form 1-A which asks them to list information about full-time employees and part-time employees, not about their use of independent or freelance or talent. So in light of some of these trends, it seems like there's a current information gap for investors because as more independent professionals and freelancers are being used and they're not part-time employees I think it could improve just transparency in the market, generally demonstrate to investors when companies have the necessary talent in place to grow and certainly allow researchers to better understand how independent talent is now supporting more of the growth of early-stage companies. So that's all for me. Thanks Carla.

MS. GARRETT: Thanks Brian, and thank you for those suggestions that maybe we can be talking about later on today. Youngro.

MR. LEE: Hello everyone. My name is Youngro Lee. I'm the founder of an investment fund NextSeed which focuses on business financing which has joined a different platform called Republic (audio drop). In terms of what we see in the market and especially investment crowdfunding and Reg A just the way the job market understands equity crowdfunding it's happening. And for sure given all the challenges we have with the macro environment and also the overall let's say non-economic events such as geopolitical events, I mean, those are all part of investor psyche, and so that's why the level of activity is showing some changes compared to maybe six months ago.

Having said that I think that the entire purpose and premise of Regulation Crowdfunding and alternative investment models is that there is potential for capital that is not I wouldn't say as impacted by the macro events as much as they care more about specific companies or locations or type of projects that are indifferent to some macro events.

The Regulation Crowdfunding investment

platform will last several years I think especially given the amendment in .31 has made a very, very big difference and I think will continue to provide at least some support to the early-stage financing market. However, as you think about how does this continue, some of the comments that was made in the earlier part of the session about liquidity, secondary markets, different tools and mechanisms that will enable participation that's what needs to be solved.

And the one thing that I want to highlight is when anyone kind of thinks about these things it's never simple. That's obviously stating the obvious. But when we talk about secondary markets, you're now entering into or requiring things like transfer agents, ATS, different kind of securities laws for secondary exchanges all of which frankly again was not built to handle transfers of let's say small securities, small private securities. The biggest issue is that the intermediaries that are able to support and help the small businesses and startups continue this process it's very challenging for them as well.

I believe you're going to see the same level if not more of those challenges in the secondary context or liquidation context. So to the extent that we want to encourage the overall industry by creating liquidity options and secondary options I think just as much options and attention should be focused on what is the infrastructure big and small that can help facilitate those secondary and kind of other infrastructure. Thank you.

MS. GARRETT: Thank you very much, Youngro. Sara.

MS. HANKS: Okay. Thanks. I'm Sara Hanks. I'm CEO of CrowdCheck and managing partner of Project (audio drop). Together we provide compliance and legal services for online capital formation. So the companies who list on platforms like Republic are obviously super early-stage companies. We are seeing a bit of a slowdown in online capital formation. I think there are several different factors feeding into that. One is obviously the general conditions and people being nervous. Also there's possibly -- we've seen a bit of a significant drop-off in Regulation Crowdfunding in very recent times.

I wonder if that's just because everybody's going on vacation when they couldn't for the last two years. I'm hoping that that's part of it, but I also think that part of the impact on this market is the crypto winter as people are calling it because there is at least anecdotally from our point of view there is a clear connection between the people who do the investing on the crowdfunding platforms and the people who do the investing in the boards, yacht club and the like. And if you have lost all your money on a stupid NFT you are possibly not going to have so much money to invest in a regular company. I'm just speculating, but we do sort of see that from an anecdotal point of view.

Interestingly, we are seeing some our clients who had been flirting with SPACs returning to the Reg A market because there's no SPAC money for them now. We're seeing a fairly significant drop-off if you look at KingsCrowd which is a very useful resource for data in the Reg CF space. You're seeing generally people investing crowdfunding commitments as something like 35 million, 36, 30 whatever. Big jump up in April which is a usual thing in our market. Many campaigns end around the end of April, so would you expect to see an uplift. Then you're seeing a downturn in much more recent months.

When we look at Reg A, it is really difficult to find equivalent data and to build on what Commissioner Crenshaw was talking about. This is an area where really some data would be very, very useful. The only way we can get data on Regulation A is to go into companies -- and what we're looking at here specifically is how much money are people raising, which is a really relevant question. Everybody wants to know the answer to that. The only way you can get this information go into the filings that are being made, the 1-Ks and the 1-SAs, look at the cashflow statement, see what's raised there, crosscheck that against the MD&A. Crosscheck that against what the company has said in Part 1 of its filing, and that is a hugely difficult manual process.

If we could have some kind of information about -- if we could have a streamlined or machine searchable source of information about Regulation A, I think that would really help all of us. And that's all I have.

MS. GARRETT: Thank you very much, Sara, and we look forward to hearing from you later on about some of the issues that we're going to be discussing today. So it is my turn. As people know I'm a corporate securities lawyer. I work primarily with very early-stage small companies. Many of these are pre-BC. I'm going to have a much limited dataset compared with others such as Catherine, Jason, Sapna and Sara.

But I would say my experience is similar to Greg's -- he's also a corporate attorney -- in terms of what I see with respect to small business capital formation. I am seeing that small companies are having a harder time accessing capital in both seed and BC capital in 2022 than in 2021. The deals are taking longer to complete, and there is more diligence, also having to rely more on friends, family and personal funds, and, in addition, liquidity events are occurring more often through M&A transactions.

And then to echo Hank's point I want to say thank you, and we appreciate the Committee members and the Commissioners that have small business backgrounds whether through personally or through their families. As a third generation small business owner I understand intimately the issues that small business encounters on a day-to-day basis and in accessing capital. And with that I'm going to turn it over to Bailey.

MR. DEVRIES: Thank you, Carla. Bailey DeVries. I serve as the head of the Office of Investment and Innovation at the Small Business Administration. We are responsible for managing the Small Business Investment Company program, the SBIC program that licenses private equity and private credit funds that invest exclusively in domestic small businesses.

Currently we have oversight management of about 30 billion in AUM. Over time the program has been responsible for the deployment of close to $120 billion in capital. In addition to that program our office oversees and manages the SBIR program, the Small Business Innovation and Research program, which works with 11 federal agencies to provide non-diluted funding to the earliest of innovative ideas.

So for my comments today I thought it might be constructive to focus on two things. One is what we are seeing across the SBIC program so across the portfolios of the funds that we manage and some of the trends that are relevant as we talk about secondaries, and then outside of that I did want to share something that informs my thinking about secondaries to a great degree.

So very fortunate to have had an incredible grandfather that was chairman of the Chicago Mercantile Exchange twice over and a father that wrote some of the earliest software, back office software for futures and derivatives trading used by futures market across the globe.

And I bring this up because when we think about the secondary markets I think there's a strong pattern and parallel with the futures and options markets in the 1980s and early '90s when you talk about a market that is heavily relationship based where there's not a great deal of price discovery to a market that moves to be more efficient through the use of data and technology to enable price discovery and efficiency.

And when we talk about equity investment either directly in companies or through funds, in many ways it is a futures contract, so you have the option or right if not obligation to hold the security at a future price. Today what we can probably agree on is that part of that equation is working, but the rest of it is not due to the lack of full price discovery.

So I think starting to frameshift and rather than thinking about private equity markets as parallel to public equity markets starting to consider them more like futures and options markets may present us with some helpful tools to consider how do we approach secondaries.

And looking at issues that have been raised such as can we get more consistency in terms of our financial contracts to make this easier? How do we think about the role of intermediaries? But the funds in some senses are intermediaries, but to an earlier point in many geographies the small funds might be more akin to what we think of as companies and businesses, and the small business startups they're inverting in are more akin to R&D projects that traditionally you use see in larger companies.

And then the fund to funds and other separate account providers have another role as an intermediary to diversify and provide downside risk protection to investors who cannot assume a certain level of risk.

So I share that as a framework that I think warrants more conversation. In terms of what we're seeing across our broader portfolio of funds that we work with, not surprisingly we are seeing some elongated durations, and it is causing more questions about the need for follow-on funds for GP-led restructurings, and how do we think about being supportive of small businesses throughout their life cycle if the duration of investment is longer than anticipated and therefore a greater need to be able to support secondary transactions such as GP led restructurings of these funds so they can launch follow-on funds, and they can continue to be supportive of portfolio companies. So with that I'll close my comments out there. Thank you.

MS. GARRETT: Thank you, Bailey, and thank you for that perspective and ideas to think about the framework. Greg.

MR. DEAN: Carla, thanks. Good morning to everybody, and I apologize in advance. My internet has been a little spotty this morning. I just want to say that this has been a great conversation so far, and there's a lot that's happened in the markets particularly over the past year. I know from FINRA as I mentioned during the last meeting we released our snapshot of our member firms that we oversee for 2021, and there was a silver lining in that in that since we start collecting numbers on crowdfunding portals and our capital acquisition brokers who are focused on the number of broker/dealers who are focused on capital acquisitions both hit record numbers last year.

So we have the greatest number of crowdfunding portals that were established since the Jobs Act. In addition, we had the highest number of capital acquisition brokers. However that was before the market conditions earlier this year took place, so we're continuing to look at this and follow this.

In addition, there were big changes in the over-the-counter market at the end of last year as well implemented by changes by the SEC. So FINRA stands ready to work with the committee members here as well as with the SEC at looking and revising rules and guidance. In fact, we have been issuing guidance particularly with regard to Reg A and smaller offerings. We just placed some guidance on our website recently, so please take a look at that.

There are going to be changes coming up, big changes for small business capital formation. And so as I said, we stand ready to work with you. I also want to mention that we also testified at the Senate Banking Committee hearing last week. We're looking at scams as well as how to protect investors. The head of our Investor Education Office, Jerry Walsh, testified. We also had some testimony which was very good.

A lot of these issues and a lot of what we're seeing are with senior investor protection, how do we enhance that as well as what's happening in the unlicensed and unregulated space. I think FINRA with regard to what we're doing and what I've heard from some of the members is it helps if everybody is on an even playing field. They know what the rules are and can work within those rules. And so let's see how we can work and improve that and give out more guidance where needed. Thank you.

MS. GARRETT: Thank you, Greg, and thank you for those perspectives. Robert.

MR. FOX: Thank you, Carla, for the time. For those of you who don't know me, I'm a partner at Grant Thornton. I serve on our audit leadership team. When I look at our client base as it relates to capital raising, I think all the themes that have been discussed so far are present especially anything that's a longer duration investment and is suffering. Biotech is one that I know a lot of our clients in that space are kind of struggling for the funding right now and definitely seeing -- that's kind of a much more longer duration investment.

Honestly, though, I think that that is much more a reflection of the economy, the level of uncertainty, the political events in Europe and, frankly, the rise of interest rates as much as it is any sort of structural issue that I see right now. I do see similar to what Greg said at the beginning a lot of capital flow especially going to follow-on deals right now but kind of that initial funding.

That funding when you don't have a recurring revenue base -- a subscription based model or some sort of annuity type of cashflow model definitely is suffering right now, but I do think that that's as much what's going on in the economy as it is what is going on in the regulatory markets.

And the last thing I'll say again echoing another theme is human capital markets, you know, just labor, finding talent, source of talent, retaining talent continues to be a massive challenge for all sorts of companies but especially smaller companies who don't necessarily have some of the human resource and other expertise to really help them think through that. And so that is, I think, continuing to be a pressure point for businesses and a continuing issue.

But again I'm not -- at least from my vantage point I'm seeing a lot of economic uncertainty. I think some of our clients are already seeing early signs of a recession or at least slowdown. I think others are still dealing with inflation issues, but to me I'm seeing a lot of economic factors facing -- creating a challenging capital raising environment, but I'm not really seeing structural issues right now beyond the things that we've talked about previously as a committee. Thanks, Carla.

MS. GARRETT: Yeah. Thank you, Bert, and thank you for bringing up the human resource issue. That's an important one. Donnel.

MR. BAIRD: Hi everybody. Good morning. I'm Donnel Baird. I'm one of the newer members of the Committee. I started a climate tech, a technology startup called BlocPower. We decarbonize buildings and whole cities. We have contracts with the city of Iska and the Menlo Park to decarbonize every building in the city within the next (audio drop) years.

I want to talk about climate tech capital formation, what we're seeing in startups and small businesses and then talk a little bit about women and minority-owned, and I guess I threw in there geographically segregated businesses that are removed from the coasts. So in the climate tech capital markets what we're seeing is that a lot of the traditional institutional venture capitalists have a lot of dry powder. Climate tech, you know, fundraising from a venture capital fund perspective is still moving pretty aggressively in 2021 and pretty aggressively, and so there's lots of investors with lots of capital to deploy.

The quality of deals and actually the size of new climate tech deals that gets done has increased. The volume of deals or the rate of increase of the volume of deals has started to decrease. And in climate tech, it may be a little bit different from other parts of the small business economy where a lot of the de-risking that needs to occur is unlike traditional software based venture capital and unlike traditional small business capital formations in that there's more CapEx upfront, and there's actually risk on the CapEx, and you can't securitize or collateralize against the CapEx in the same way. So it's a little bit of a unique moment.

What we're seeing my firm is raising I want to say like 30- to 40 million of venture capital. It's taking a little bit longer than I would have liked. I can't tell if that's because I'm black or if it's the broader markets. It's always confusing. But venture capital is still pretty racist, still pretty sexist, still pretty geographically constrained. Our transaction will probably get done in the next two to three weeks with the first closing today or tomorrow. So we're very fortunate.

And I think again for climate tech firms that have been around for a few years and have been de-risked we are able to organize larger pools of capital. We actually are doing a Reg CF offering and a Reg A offering right now as well, but we are not offering equity shares. We're offering debt shares. And I think this might be relevant to the secondary piece because one of the things we're seeing -- one of our investors is Microsoft, and one of the things they're really interested in is like they can get, you know, financial returns from a lot of different places.

They're too big to really underwrite an equity check of, like, $3- or $4 million, but they will do it for debt, and they are really interested in doing it for debt that's connected to carbon offsets or environmental justice offsets. And so the additional value when tied to a security seems at least from the perspective of a Microsoft during Apple or a Google, who were our first three customers, is like they're willing to buy and almost create a secondary market for our BlocPower debt securities provided those debt securities are tied to the social and environmental impact or carbon reduction impact that's being generated through the use of the debt.

And I just think that's interesting because if you tie that social or environmental impact component to the security, how might that change the appetite or the market for secondary transactions that have been de-risked. And in our view, if you de-risk a security and add that social and environmental impact, we think that's really powerful particularly when you start thinking about capital formation for small businesses in the supply chains of companies that have going to have to do climate disclosures according to the new rules that we're talking about which is very exciting. So that's one part.

The second part is I'm on the small business board for the New York Fed, and one of the things we talk about is after the last -- after the 2008, 2009 economic collapse that the counties across America that had the quickest financial recovery from that financial collapse was highly correlated with women-led neighborhood scale non-venture backable e-commerce business. If you think some somebody who's like a local baker, and they're like, “Hey, I'm going to have an e-commerce bakery,” a venture capitalist is not going to invest in that business. It's not venture scale.

But those women-led and in particular minority women-led e-commerce businesses at neighborhood scale were the most highly correlated indicator of an American county that recovered most quickly after the last recession. I just think that's really important for us to continue to focus on because of course those are exactly the people who cannot go to venture capital because it is racist and sexist, and it is tied to the coast, and the checks are too large.

So thinking about how SBIR or SBIC funding could be reorganized in order to not have, you know -- at the wall and hopefully one of your ten portfolio companies works out and gets to venture scale and recovers the losses of the other nine. But what does it look like to invest capital in micro venture or micro private equity scale for women-led, minority-led e-commerce businesses who need $20- to $50,000 a pop, and instead of nine of them going out of business maybe only three or four of them go out of business. So your returns are going to be lower, but your risk is lower. And is there a different kind of market that we can create?

And again if you can start to monetize and quantify the social environmental impact whether it's local jobs created, or what have you, is there a potential secondary market that would be generated for those kinds of debt or equity securities? Thank you.

MS. GARRETT: Thank you very much, Donnel. Appreciate your perspective and insights into that. I want to thank all the committee members today for sharing their thoughts. I think we have a broad range of diverse experiences, and I personally think it's quite useful to hear from people especially in this virtual age right now about what people are going through in their different sectors. So I really appreciate everybody giving thought and time to their comments today, and I think that was quite useful. I hope others do, too.

So now we are going to turn to our second agenda item. I'm going to the say the words secondary market liquidity a lot. So we could play a game here, but let's go ahead and start.

Today we will be discussing secondary market liquidity for investors in Regulation A offerings, crowdfunding offerings and smaller public companies and the secondary market liquidity challenges that the private and small public companies and their investors encounter.

SECONDARY MARKET LIQUIDITY FOR INVESTORS IN REGULATION A AND REGULATION CROWDFUNDING COMPANIES AND FOR SMALLER PUBLIC COMPANIES

MS. GARRETT: As we know, secondary market liquidity is integral to capital formation, that there are barriers to secondary market liquidity, and capital may be more expensive and more difficult to secure. And as Commissioner Peirce pointed out illiquid companies may have a harder time attracting companies. Today I hope that the Committee will explore whether there are changes that could help facilitate secondary market liquidity for these investors.

In addition, we will discuss if going public solves the liquidity problem for investors in these small companies, and we will hear how investors in smaller public companies also face liquidity challenges. But before we turn to our speakers we thought it might be worth starting with a general legal overview which may take some of you back to your first securities law course.

The Committee has talked a lot about the initial offer and sale of securities from a company to an investor, and we know that foundational aspect of the securities laws is that every offer or sale must be done through a public offering with the SEC or in reliance on an exemption from registration which is Reg D, Reg A or Reg Crowdfunding. That initial sell is a transaction that most people think about in connection with capital formation. However, in areas that the committee has not spent as much time on but which is also a key component for capital formation is what happens when those initial investors seek to sell their shares in the company?

When investors seek to exit through secondary market sales, selling shareholders must also comply with federal and state securities law requirements just as issuers must do so in initial transactions. Our speakers will cover this more thoroughly today, but with respect to the federal securities laws many selling stockholders that are not affiliated with the company can rely on a federal exemption from registration that does not require a securities filing for such sale.

For example, this is mentioned every time a selling stockholder of a public company sells a security to a new stockholder. However, with respect to the state securities laws, often the bylaws, this is different. Generally, if an issuer filed ongoing '34

Act reports or listed on an exchange, then federal securities laws preempt state securities laws for purposes of security sales. However, if a security is initially sold pursuant to Regulation Crowdfunding or Regulation A, federal securities laws do not preempt state securities laws for purposes of secondary sales.

So we will hear today some of the challenges that Reg A and Reg Crowdfunding investors face when navigating state securities laws for these secondary sales. Today I also hope to hear more about what broader exit opportunities there are for investors specifically in Reg A and Reg Crowdfunding deals where the companies continue to provide the public with ongoing reports.

I'd also like note that the topic of secondary market liquidity is not new and, in fact, was considered by the predecessor of this committee in 2017. That committee provided the recommendations to the Commission with respect to reducing the friction for these types of secondary sales. Secondary market liquidity is also timely since legislation is circulating on the Hill that would attempt to address secondary liquidity challenges for Regulation A and Regulation Crowdfunding investors.

With that in mind we will now turn to our invited speakers. First we have with us Ryan Feit, the

CEO and cofounder of SeedInvest, one of the first equity crowdfunding platforms following passage of the Jobs Act. In 2019, SeedInvest was acquired by Circle, a global financial technology firm, and the platform continues to operate.

Prior to founding SeedInvest Ryan worked at Wellspring Capital Management and Lehman Brothers where he financed and worked closely with many private and public businesses.

And next we welcome Joan Adler a partner at Ellenoff, Grossman & Schole, LLP. Joan specializes in state Blue Sky laws and broker/dealer regulation. She works with public and private companies as well as underwriters and placement agents on state law exemptions and registration for initial, secondary and private offerings. In addition, she advises investment advisors on exemptions and registration on both the federal and state levels.

Ryan and Joan, we appreciate each you taking the time today to be with us and your willingness to share your expertise and your perspective. I will now turn it over to Ryan.

MR. FEIT: Thank you, Carla, and thanks all the members of the Committee as well as the Commissioners for having me today. I'm going to attempt to share a slide deck. Hopefully this works. Somebody can let me know. Are you able to see my screen?

MS. GARRETT: Yes.

MR. FEIT: Excellent. So for starters I just want to share this screen, this deck. The information included is really for informational purposes only for this discussion. I'm not going to spend a lot of time on myself. I think it already was well done. But in addition to being involved in the Jobs Act and founding SeedInvest I'm also a board member of Crowdcube, which is the largest equity crowdfunding platform in the UK and Europe. So I have a pretty decent global perspective on some of these issues. And I've also served on FINRA's Fintech Committee since it was founded about five years ago.

Just a quick overview of SeedInvest. We were, basically, founded in conjunction with the passage of the Jobs Act, started doing our first deals in early 2013, and today SeedInvest has over 700,000 investors and have invested in hundreds of companies over the years.

So for starters, I wanted to give a quick snapshot of the current state of online fundraising from our perspective. This has been covered a little bit. I think at a high level the Jobs Act has enabled millions of Americans to be able to invest in startups and small businesses for the very first time, and in addition this has provided thousands of entrepreneurs with a new way to access capital. So I think that's all tremendous, and I think the Jobs Act has been serving those needs fairly well.

And we believe that this new online source of capital is very important in times like today. We've seen over the last ten years during times like the beginning of COVID when things froze up and in a few other periods over the last ten years that when traditional sources of capital like venture capital as some of the other members of the Committee have already mentioned start to freeze up and market environment like we're probably going to experience over the next year or two, a lot more entrepreneurs actually frequent platforms like SeedInvest to raise capital nontraditionally. I think it's a really important time for it.

I'd also add that -- I know this was mentioned before, but Regulation Crowdfunding has become much more useful since recent improvements to the Jobs Act kicked in a little over a year ago namely the increase of the cap in Regulation Crowdfunding from 1 million per year to $5 million and some other smaller improvements.

Regulation A+ from our perspective continues to be I think adopted more and more by high growth more established issuers I'll talk about in a minute.

We see a lot of companies that will raise their seed rounds through Regulation D or through Regulation Crowdfunding, and then as they sort of mature they'll go on and raise larger rounds through Regulation A+. A good example of this is a company called NowRX, and I think this is -- NowRX is a great example of the fact that startups can actually now leverage these exemptions that were legalized as part of the Jobs Act to raise capital purely through online fundraising nontraditionally.

And so NowRX came to seed invest back in 2017 and 2018 and raised their seed round through Regulation Crowdfunding and Regulation D. They came back in 2018 as they grew and raised a $7 million Series A Regulation A+. They came back two years ago and raised a $20 million Series B from 9,000 plus investors on SeedInvest Regulation A+, and then a few months ago they actually closed as far as you know the largest sort of online equity crowdfunding raise in the country, which was a $27 million Series C from 9,800 investors.

So I think it's tremendous to just see. This is something that I think ten years ago is probably hard for a lot of people to fathom when we were sort of writing the Jobs Act and discussing it. So it's pretty powerful to just show the possibilities of these exemptions in online fundraising and the possibilities for investors to be able to participate, but it also begs the question. With this many investors, what happens to the investors and where is the liquidity? which I'll touch base on in a minute.

Just continuing, on the primary perspective, primary being just primary fundraising capital, over the years there does seem to be a relatively healthy balance that we sort of struck with the Jobs Act between expanding access to capital for entrepreneurs and providing access for investors while ensuring adequate investor protections. I will say every platform has very different standards. Every platform is not created equally. Everyone has different ways that they handle these.

Beyond the primary raises themselves we see two major outstanding hurdles to making online fundraising and investing really viable asset classes for the mainstream. The first is diversification. One of the problems that we continue to see is that a lot of retail investors will come to platforms. They'll make one investment. They'll make a few investments, and that's it. Obviously, this is important. Diversification is mission critical in the public markets. Most people invest through things like ETFs nowadays and are passive and build a diversified portfolio, which is great.

This is even more important when you're investing in private companies given the high rate of failure. I think it's a problem that does not have an easy solution today. I have some suggestions around it. But separately the second issue, which is probably the focus of this conversation is liquidity. Investing in a company it's great that people have access, but investing and exiting are two very different things, and this remains a significant problem along with diversification.

Why is this a problem? I think a lot of commissioners and committee members also touched on this, but what happens is many startup and small business investors get burned out quickly. They make an investment or a few, and they're excited about it, and then they actually realize that I might need to wait five to ten years to get any return out of this. And although some of these investments on paper might appear to be doing well because companies are raising rounds at higher valuations five to ten years is a long time for people.

And so this ultimately -- you know, the results of this is simple. Without liquidity this ultimately leads to less capital available for startups and small businesses.

I think one point of good news that I wanted to provide some data on is that ten years ago when we were sort of working on the Jobs Act there was a lot of skepticism around the Jobs Act. There's still some today, obviously, but there was a lot of skepticism that any investor would actually realize any returns from investing with the online platforms, and there was a lot of thought ten years ago that only the worst possible companies would come to raise capital online, and it would be only the worse possible opportunities for investors.

The good news is that we actually have some case studies now of examples where retail investors were able to invest in startups and small businesses for the first time as part of the Jobs Act and cases where they actually have done well. So I just wanted to sure a few of these, and these are examples.

So the first this is a company called Heliogen. They raised capital through Regulation Crowdfunding back in 2017. It was founded by a very well-known entrepreneur named Bill Gross who founded IdeaLab 30 years ago or so. So he's very well known in the Valley, and he, basically, raised about a million, six on our platform in 2017, a $20 million valuation. There were 900 plus accredited and nonaccredited investors who participated in the raise, and about four years later the company went public at a $2 billion valuation. And to our knowledge this is sort of the first retail investor unicorn exit in the United States.

These investors, it depends on when they sold their shares, and everything like that, or whether they're holding, but they, basically, had an opportunity within four years to, basically, to generate a return of 28 times their money. This is just something that I think is a powerful example of something that nobody -- not nobody. I obviously did because I started SeedInvest, but a lot of people were very skeptical that retail investors would ever have this kind of an exit through an online platform. So I think it's powerful.

Another quick example is a company called Nightscope. We, sort of, did part of their seed round back in 2014. We did a subsequent $20 million Reg A+ that 4- or 5,000 investors participated on. They went public under Nasdaq earlier this year, and the returns for the people on our program were quite well, or were quite strong as you can see on the bottom bullet.

I'll breeze through a couple of these other ones because I want to get into the meat of this. TrustStamp is another example of a company that did a Reg A+ offering on our platform and then, basically, a little over a year later went public on the Nasdaq. And investors also, depending on when they sold, did quite well with an IRR of approximately 90 percent. Shelf was a company that did a Reg D offering back in 2016, and people, basically, would have generated a return of almost 100 percent IRR or 22 times cash-on-cash. PetDesk also a Reg D offering, more results here. I'm not going to spend too much time on these.

I just wanted to flip through a few of these. Again these are examples. This is not, obviously, the data on our entire portfolio, but I wanted to show just some actual data on the fact that there is a potential for investors. The vast majority of America who has been until the Jobs Act sort of prohibited from participating in investments and startups and small businesses is actually doing well, but as you would guess the vast majority of companies that have raised capital through Reg CF, Reg A+, obviously Reg D as well are still -- are sitting on investments that on paper might be doing well but have no liquidity. That's the majority of the companies in the space, and this is a huge issue.

So I wanted to talk about a few of the challenges that we see. Some of these have been already talked about, so I won't spend as much time on them, and I want to talk about a couple potential suggestions. Challenges with the secondary market liquidity today for early-stage, startups and small businesses there obviously are existing trading venues out there. There are none, at least in our opinion, that are built for early-stage companies and that have the necessary liquidity and research coverages to provide sort of the right experience for early-stage company investors. So that's an issue.

As I think a lot of people probably know today startup and small business investment documents typically include prohibitive clauses like a right of first refusal which makes secondary trading challenging and far less efficient. So I think part of this is there are regulatory changes that we could make that would make it much easier for there to be a vibrant secondary market.

But in addition to that, in addition to the regulatory and the infrastructure we also need to sort of work with the sort of legal counsel networks of these companies and work with entrepreneurs to remove some of these prohibitive causes in order for this to all work. So there's a few different levers I think we need to focus that make sense.

This has obviously been touched on already, but as was mentioned Reg A+ preempts Blue Sky laws for primaries but not for secondaries. Reg A issuers must already comply with extensive ongoing public disclosure requirements despite the fact that Blue Sky still exists. You have to go state by state unless you have an exemption.

And then the last thing I would mention is with some of the companies that we've seen go public the share transfer infrastructure with transfer agents and the like are just not built today for these small company public listings. And so because this infrastructure is very archaic and not really set up for these sort of smaller companies what ends up happening is you have a company that goes public, and there end up being significant delays for investors to actually get their shares maybe deposited into their Schwab account, or whatever it might be, and then to actually sell their shares.

And sometimes you can sell through computer shares, but it's very expensive and very clunky. So what this ultimately can result in is these investors sort of losing a lot of value as the share price moves by the time it takes them to actually get access to their shares. So this is something that I think hasn't been discussed which is an issue.

A few suggested improvements, and then I will hand it over to Joan. This isn't talked about, but we agree that -- and I know there will probably be a conversation on this, but we agree that state securities laws should be -- Reg A issuers should be preempted for secondary trades as long as they're current in their ongoing reporting or -- and we sent a comment letter to NASAA a few years ago on this as well -- or we need to really push further amendments to the current NASAA requirements and actually make sure that all states adopt those, which is easier said than done, I know.

Secondly, and this is something that I've heard anecdotally from some folks in the space, but that there seems to be a need for additional clarity for brokers and clearing confirms that Reg A+ reporting, basically, satisfies 15c2-11 and that shares are free to trade immediately. I've heard that some sort of compliance departments whether it's in the Schwabs of the world or Fidelities, et cetera, remain skittish and so sometimes investors have a challenge depositing their shares right away when a Reg A+ company goes public.

Third is that I do think, and this touches on some of the challenges with the transfer processes but also a lot of other challenges that I see with secondaries is that -- and I know this is a big one, and we're not going to answer this one on this call, but additional regulatory guidance around permissible ways for issuers and broker/dealers to leverage digital assets and just distributed ledger technology to make secondary trading more efficient.

I know this is a big one. I know there's a lot that needs to be figured out. I don't have all the answers, but I do believe that Blockchain technology can provide efficiencies around secondary trading in a number of ways.

The last one, this kind of like a moonshot, which is a longshot here, but this is something I mentioned at I think one of the SEC annual meetings a few years ago. Actually, Catherine alluded to some of this as well herself. I mentioned this before. Investors in the public markets invest and diversify by products like ETFs, and they're passive, and they have a diversified portfolio.

And I think at the end of the day with startups and small businesses I think 80 percent of people probably should be investing passively as well in a diversified vehicle and just making the decision I want to put 5 percent my savings into venture capital and do it for me in a diversified way versus picking and choosing these different companies.

And that is very tough to do especially with nonaccredited investors. There's not really any vehicle that I am aware of that's easy to facilitate that for nonaccredited investors aside from basically registering under the '40 Act and getting qualified by the SEC which is very expensive and not really -- not a fit and has a lot of challenges around mark to market and things like that.

So I think that if there’s a way to leverage Regulation A+ and amend the Investment Company Act to provide a mechanism for a diversified venture fund that nonaccredited investors as well as accredited could invest I think that would provide a silver bullet for providing diversification for investors. When you invest in a fund as well because you're diversified some of those investments end up having liquidity earlier than others, so it mitigates the liquidity risk to some extent.

And then lastly, at the end of the day this would actually we think improve the quality of the offerings available to retail investors quite a bit. I could spend more time talking about why people want that, but I still think that some mechanism for retail investors to easily diversify these investments is missing, and I think that's an important thing that I just haven't heard a lot of people talk about and I haven't seen proposals around. That's it from my end. I appreciate it. I'm happy to take questions right now or pass it off to Joan and then start a discussion. I yield to you.

MS. GARRETT: Thank you, Ryan. We will have more questions after the speakers, but if anybody has a question for Ryan right now if you can put yourself in the chat so I can see or go ahead and ask it just based on what you might have just heard. If not, then we will turn it over to Joan. Ryan, can you turn your screenshare off? Thank you.

MR. FEIT: Yes.

MS. ADLER: Thanks everyone. Thanks Ryan. That was a great presentation. Thank you to the Committee for inviting me, and thank you to the Commissioners and all the Committee members for their comments. A lot has been covered at this point, so I just want to kind of highlight some of the issues relative to the very broad scope of secondary trading involving Reg A issuers and Reg Crowdfunding finance issuers.

One of the things that Ryan touched on -- for context, as a partner at Ellenoff, Grossman & Schole my firm has been involved in both the early days of the Jobs Act and Reg Crowdfunding, Regulation A, the general solicitation of Regulation D offerings, so we've seen how this whole access to financing has evolved. And in the early days the focus was primarily on, as Brian has noted and others have noted, the initial offering of securities and having preemption, and so forth. But there has not been as everybody has noted as much focus on how do you get out.

So we have created these mechanisms and some really wonderful crowd finance websites like SeedInvest, like StartEngine that Sara Hanks has been involved in and many others where they have beautiful websites presenting investment opportunities for investors. In most of these situations, you just need your phone. You need a computer. You can get into these investments very easily. The disclosure documents are prescribed for Regulation A. The disclosure is prescribed for Regulation CF, but getting out of them is not as easy as getting in.

Another issue to leave aside is the concept of institutional investors. I deal a lot with Blue Sky. If you're an institutional investor, you don't have to deal with many of these state Blue Sky issues because there are exemptions for unsolicited transactions. There are exemptions for transactions with institutional investors. You have a broad road to travel if you are an institutional investor, but if you are not then you are either an individual accredited investor, or you are an unaccredited investor. Your access to getting both into and out of investments becomes incrementally more challenging.

One of the ways -- and Carla gave an overview of this. One of the things that Carla covered and Ryan as well is the secondary sale from investor to investor is not preempted, and it has to comply with state Blue Sky laws and regulations. We know that Reg Crowdfunding transactions after the first year are really broadly restricted. Reg A securities are unrestricted, but that doesn't mean that they can readily be sold from investor to investor.

And one of the things that people have relied on is the manual exemption, and this is, basically, the focus in on is there current information sufficient for an investor to make an investment decision on a sale, on an exit before a company will, as Ryan highlighted, exit into a public company, and they have the ease of the public markets. The Reg A offerings and Reg Crowdfunding offerings are not traded historically on exchanges. Only 39 of these companies at this point are traded on the OTC markets. So that leaves a tremendous amount of companies that are not traded readily available.

And so how do these investors get out? They have to look to alternate trading systems of which there are some, Templum, PPEX, some others that are around, but they're not as easy to find. They don't have the same kinds of pictures and posters that you have coming into these investments, you know, on SeedInvest, on StartEngine, on many the other websites. And the investors don't have -- where crowdfunding you only have to continue recording for a year or so, Reg A issuers also don't necessarily meet after a few years to continue their reporting obligations.

So if you come into one of these offerings and your issuer is no longer providing public reporting, how are you going to get access? Compare this to institutional investors. They have the sophistication to ask whatever questions they want. They have the weight. They have the heft to do that. But the unaccredited audience or, you know, your basic accredited inventory will not have that kind of leverage to be able to get the kind of information that they need.

One of the things that my firm has been involved with has been working on the manual exemption. What that means is state laws -- there's 50 states. There's D.C., Puerto Rico, Guam, U.S. Virgin Islands. So there's technically 54 jurisdictions. You need to look at 54 jurisdictions. You don't know where your buyers and sellers could be. And most states have an exemption. Historically, it was for Standard & Poor's manual. It used to be Moody's, and now it's Mergent, and most people don't even recognize the name Mergent. They still remember Moody's, which hasn't been in existence for a very long time. So there aren't a lot of opportunities.

OTC itself created its own manual, but its manual is solely for the securities traded on its alternative trading system. So there needs to be a mechanism, and this also ties into recent changes to Rule 15c2-11. There needs to be a mechanism for presenting public access to current public information on these companies that have the Reg A and Reg CF securities.

My company, my law firm has worked with a couple of colleagues at Crowd Finance Capital Advisors and North Capital to create a manual for exactly these kinds of companies, crowdfunding companies, Reg A companies that are not reporting as well as private companies that have issued securities under Regulation D to, basically, replicate the dataset of what you would need to present for 15c2-11 compliance, Rule 144 compliance, Reg A dataset, Reg Crowdfunding, you know, continuing reporting obligations and has worked with CPA.com and Mergent to prepare and make open to the public every securities regulator, any person anywhere any time these reports with the kind of information that investors would need because you need to address the lack of the current public information to make an informed investment decision.

And to Donnel's point earlier, she highlighted the kinds of companies that she's seeing, neighborhood companies, passion investment, women-driven businesses and other things, and that's why some of these ATSs are saying at they see is, you know, people who have gotten in and maybe need to liquidate an investment but also people who didn't have an opportunity to get in to say a Reg A round or Reg CF round, and they want to be able to come into these rounds, and they need not only the information to make the investment whether to come in or to liquidate but also, we need to make easier the venues, the ATF venues, for them to conduct these transactions.

That likewise ties into the points that Brian was making about brokerage suitability and the brokerage firms being comfortable with the datasets for brokerage transactions. I'll stop there for now.

MS. GARRETT: Thank you very much, Joan. Does anybody have questions for Joan right now? We are going to have -- just so people know, Andrea is going to speak, and so is Sara before we open this up for general questions and answers. Does anybody have anybody right now for Joan? Okay.

Andrea, just as a reminder I will -- I will remind people who Andrea is. She's our committee member who has been appointed by NASAA, and she's the Ohio Securities Commissioner, and she's going to discuss among other things the preemption issue that has been mentioned previously in this meeting.

MS. SEIDT: Thank you, Carla. I have some prepared remarks, so bear with me. Thank you Carla and Sebastian for organizing the meeting today. I have not had too many opportunities to engage with a lot of the committee members this year due to conflicts on my end, but when I have been able to participate I have tried to not be too disruptive.

Aside from dissenting footnote that the Committee graciously extended to me on the accredited investor letter I think I've been fairly quiet especially for those who know me well. So I apologize in advance had any comments today seem disruptive, but the Committee is considering action on policy that I strongly oppose, namely a committee recommendation or support for preemption of my agency's authority and the authority of all state securities regulators to oversee secondary sales of Reg A, Reg CF and perhaps even other exempt offerings.

I understand and NASAA understands that small business capital formation is incredibly important to our financial markets. I respect this committee's mission to promote it, and personally I've been moved by every small business who has joined us this year to share their capital formation successes and their struggles. I live in a midwestern town that has grown into a thriving tech and startup hub because of small businesses just like them, and while capital formation is important work it is not the only work that this committee is charged with.

Beyond capital formation our committee charter states that we are supposed to provide the Commission with advice respecting the Commission's mission of protecting investors and its mission of maintaining fair, orderly and efficient markets. Any proposal that does not take all aspects of the SEC's mission into account is not ready for the Commission's attention.

You will not be surprised to hear that I do not believe granting state authority over secondary sales of Reg A and Reg CF offerings will either, A, protect investors or, B, lend itself in any way to fair, orderly and efficient markets. I'm sure the Commission staff and other committee members like Sara will speak up if they disagree, but industry compliance with Reg A and Reg CF exemptions tend to fall on the spotty side. We see ongoing reporting, advertising violations, financial statement issues, and notice filing and fee mistakes are just a few of those soft areas.

And while we're on the topic, registered secondary sales are very likely another danger zone, but I'm not aware of any states bringing cases in that area, at least not yet. So no matter how hard those small businesses tug at my heartstrings my job as a regulator is to fairly apply the rules to all businesses. My job also requires me to protect investors from fraud and loss, and these offerings pose high risks for investors.

You heard Ryan talk about the very high

failure rate for these offerings. Investors, by the way, also tug at my heartstrings. Investors file complaints that my team is duty bound to investigate when this risks materialize. One of the risks we are especially concerned about in secondary sales is the risk that company insiders and wealthier sophisticated investors will exit bad deals by dumping their shares or more vulnerable unsophisticated investors. Our committee charter demands that we consider those risks as we weigh options today.

In addition to investor protection, our committee charter directs us to think about the larger market impact that blanket state preemption would have on the secondary space for Reg A and Reg CF deals. This impact is admittedly hard to assess because we don't have good data about the primary offerings, at least not from the investor's vantage point. We just celebrated the ten-year anniversary of the Jobs Act. I've heard a lot about how much money has been raised in Reg A and Reg CF for the past ten years, but I've heard nothing about the fail rate for those deals.

Without cherry-picking deals from the pickiest platform -- no offense, Ryan -- can anyone tell me how much money has been lost in these deals over the course of the last ten years? Can you tell me what percentage investors have made as a return on their investment on the deals that we count as successes? I am pretty concerned about what happens in the secondary market for the 98 percent of the deals that SeedInvest rejects as too risky or too low in quality to list on its platform.

I'm also concerned that portals are not subject to the full scope of laws and regulations that broker/dealers are written to protect investors like suitability and best interest. Eliminating existing state registration requirements that gives investors basic disclosure about Reg A and Reg CF at resale would make an opaque part of our U.S. securities market yet another shade darker. I would call it something like opaque squared for the investing public.

It will remove yet another incentive for American companies to list and be fairly and publicly valued. It would also increase the potential for fraud and abusive insider sales. Those don't sound like positive developments for our financial system to me.

To make a balanced and informed policy decision the Committee needs much better data than it currently has. This includes data showing that the proposed secondary market exemption will positively impact the primary market and the financial successes of the issuers and data that such a proposal would not frustrate the Commission's equally laudable goal of facilitating a robust and thriving public market.

Lastly, I worry that preemption will ultimately lead to hasher and more negative enforcement outcomes for the small businesses and other unsophisticated private market participants that I know you want to help. With this particular proposal, I worry about issuers and resellers. I know that some of you have supported -- maybe all of you has supported preemption proposals in the past because you think state registration is a bad and costly thing for issuers and intermediaries, but I see it quite differently. I believe an ounce of prevention is worth a pound of cure.

State examiners help unsophisticated issuers identify weaknesses and other red flags in their offerings before any damage is done, weaknesses and red flags that could cost issuers dearly if not identified prior to sales. We see a lot of compliance mistakes, a lot of sloppiness by issuers and intermediaries in the private market. Many times it is unintentional, just businesspeople who are unfamiliar with securities laws operating outside their lane. Other times it can be fraudulent.

We see outdated, inaccurate financials, unrealistic projection, misleading advertising and what

I would say is a consistent effort by issuers and intermediaries across the board to gloss over downside risk of these high risk offerings. These are common but damaging rookie mistakes that we don't see by large publicly traded companies.

As it stands now registration gives states like mine the opportunity to identify and fix problems early and comparatively cheaply. Without state registration, however, it is much less likely that those issuer and reseller mistakes will not be identified early on. States probably won't hear about mistakes until after there is investor harm and complaint. It will be too late for states to help the issuers and resellers then, and as I think all of you know mistakes and sloppiness regarding risk disclosure and financial disclosure are really hard for regulators to ignore, and those are exactly the kind of mistakes and sloppiness that we should expect to see in secondary sales of Reg A and Reg CF offerings.

Problems that could have been identified and corrected at the registration stage can turn into fraud cases with disqualifiers that boot some issuers and resellers out of the private markets entirely. I would much prefer state preserve that gatekeeping function to avoid foreseeable outcomes like these.

Lastly, should any of you conclude as I do that it would a mistake to preempt state registration and secondary sales is not only a mistake for investors but a mistake for issuers and resellers as well, then I hope that you will reach out to me or others at NASAA to see what we can do together to promote safe secondary sales of Reg A and Reg CF offerings, safe for investors but safe for issuers and resellers, too.

And I'm not the state expert when it comes to these issues, so I won't be the one who moves the ball forward. I work closely with the folks who will, including Faith Anderson from Washington state. I had suggested that we invite Faith to speak to you all today in order to give us a more balanced presentation of the pros and cons of the proposed preemption policy, but my suggestion was obviously declined.

I respectfully ask that the Committee defer any vote on this proposal, any preemption proposal and defer issuance of any related recommendation until Faith or another speaker who can more effective present the state options is heard. Thank you so much for your time.

MS. GARRETT: Thank you, Andrea for your remarks. Next you're going to hear from Sara Hanks, one of our committee members who has substantial experience with Regulation A offerings. Sara.

MS. HANKS: Okay. So Andrea is going to be surprised that I am not actually advocating any kind of preemption this time. I am just going to kind of bring all of the conversation together and try and put it in context because I think if you're watching all of these presentations and you're a layperson there's a lot of context that you don't have. So I was going to walk it back to really some of the first basic principles of how the states and the federal laws work together.

First, though, I just wanted to address one point on the data issues. Both Commissioner Crenshaw and Andrea have raised issues with respect to data. With respect to what Andrea had said, not only can we not measure what people have made we can't even measure what people have raised. I would love to see another report along the lines of what Dara (phonetic) did a couple of years ago with respect to the exercise I mentioned earlier where we go in, we look at the ongoing reporting for the various companies and find out what was raised because without knowing that it's difficult to sort of fast forward to okay, and what happened then.

In many cases, and again I don't know if Andrea is going to be surprised, yes, there is incredible sloppiness. There is a huge amount of noncompliance of the primary and the secondary level, and some of it is actual outright fraud. We do see a fair amount of complete fraud in certain Tier 1 offerings, and I am forever giving people the heads-up on what we have seen.

Building on what Commissioner Crenshaw had said with respect to only 75 percent of Reg A is -- sorry, 75 percent of the Reg A companies aren't trading that's a very distorted number because if you include the OTC reporters that is going to completely skew the results. Basically, from a data point of view, there is almost no real trading of the real Reg A companies, and the OTC companies some of whom are misusing Reg A are skewing that data, as I said.

But to circle back to the very basics here and how we got to this conversation, starting point all transactions in securities, as Carla said, have to be registered or exempt whether it is Unicorn, Inc. selling to the public in an IPO or whether it's me selling to Carla in a private transaction every transaction has to comply with the registration provisions of the Securities Act and relevant state laws.

So for every transaction primary or secondary you've got three options. They can be registered, they can be offered in an available exemption, or they can be illegal. Preferably you take one of the first two. Same applies to both federal and state law. Same options. Now, as we know, in primary transactions this is the issuer selling to the public. The exemptions from registration at the federal level include Regulation D, Regulation A, Regulation CF Crowdfunding and Rule 701 and then a few other dogs and cats.

But not only do you have to comply with the federal register exempt rules but the states unless state law is preempted, and what “preemption” means is there's a statutory provision that says this transaction isn't -- it can't be subject to the registration or qualification or equivalent provisions of state law. The SEC can't preempt state law. There has to be a statutory authority, and we will discuss Reg A statutory authority in a second.

But there is some form of preemption for primary offering for all three of the primary exceptions. Remember when I say, “primary exemptions,” Regulation D, Regulation CF, Regulation A. The cleanest preemption is a clear statutory preemption in Section 18 of the Securities Act with respect to Regulation D-506, Rules 506 which comes in two different flavors, but those offerings are preempted from state regulation.

States can't require registration or

qualification, but they can require notices to be filed. Most notices do have state notice requirements which, by the way, you are required to comply with and which, by the way, building on what Andrea said about the sloppiness, we see that being failures in compliance all the time.

In contrast to Reg D, Reg A is probably the least clean preemption for primary offerings. The statute improving Regulation A so that it is now called Regulation A+ by many the statute said that the SEC can designate some investors with respect to there is preemption, and the SEC says, okay, it's all of the investors that we are offering to. It was controversial to say the least at the time. However, there was a lawsuit. The SEC won.

Where we are at the moment there is preemption for primary offerings under Reg A. State notices and filing fees are permitted, though. Regulation CF there's a preemption for all offerings under that exemption. State filing notices are permitted under limited circumstances.

So quick note on how some of that works in practice especially with Reg A. We've seen some challenges because all of the states have interpreted the Reg A provision slightly differently. So we have in the past had to produce paper filings of what we filed online with the SEC and put them in an envelope and send them through the mail to some states. I think we solved that one now, but that was fairly burdensome.

Some of the states have different timing requirements with respect to when the state notices need to be filed, so coordinating filing with the states with the qualifications of a Reg A offering with the SEC is a bit of a challenge. Some of the states say it has to be 21 days before a sale. Some say 28 days before a sale. They have different rules with respect to renewal requirements. Do you file once for an offering which can be open for three years, or do you have to renew on an annual basis?

And then in some cases states have variable fees which means if you sell more in Texas you've got to pay more in Texas, and so that can be a practical challenge. But all of that you can cope with at least on the primary side. It is the secondary aspect of regulations that leads to the real challenges that we're seeing and some of the things that Joan and Ryan have flagged. As Carla said earlier, at the federal level with respect to a secondary sale there is an exemption for anybody who is other than an issuer, underwriter or dealer. They can resell at the federal level.

When Mrs. Jones resells her shares on the New York Stock Exchange that's the exemption that she's relying on even though she doesn't realize that she is. And then you've got federal statutes that provide that a Section 4(a)(1) sale on a national securities exchange is preempted from state regulation. So trades from listed securities on the New York Stock Exchange, Nasdaq, no problem, but for non-listed securities such as on the Alternative Trading Systems, or ATSs, which Joan mentioned earlier you have to comply with the regs of the state in which the transaction is effected both seller and buyer even for companies that are registered with the SEC.

Every state has got a patchwork of different exemptions. You've got sales to accredited investors. And to build on what Joan had said earlier for institutions not such a big problem because most of the big ATSs rely on exemptions for sales to accredited investors which can come in two forms. There were state exemptions, and then there's a federal exemption, Section 4(a)(7) which does preempt state regulations for resales, but it comes with all sorts of conditions. So trading among institutional investors usually relies on those.

Then you have something called isolated non-issuer transactions for just a random Mrs. Jones wants to resell. So she can rely on the isolated non-issuer transaction, but there is variance among the states on what “isolated” means. Diving a bit more into the securities manual that Joan referred to there is an exemption in many states, not all, for transactions in securities that appear in a securities manual. As Joan said there used to be a few of these. Now it's just essentially Mergent, but even getting into the manual comes with bells and whistles.

Several states have additional requirements on top. If you are going to rely on the securities manual exemption, in some cases, you will also have to have an audit, and in some cases you can only be reselling if the company is of a certain age. Bit of actual commentary. This is me commenting here. When you look at what goes into the securities manual it's not what I would look at in making an informed investment decision. There is some financial information in there. It is not as good as a good compliant Regulation A ongoing report.

Other exemptions that can be relied on for secondary resales include some states treat Reg A reporting companies as the equivalent of being in the manual, but even then there are additional requirements. Some of them require three years of operations plus $2 million in assets. There's a couple of dozen states who provide that.

Then we have a few miscellaneous exemptions such as piggybacking on Rule 15c2-11 that Joan mentioned earlier, and then we have California who does their own thing. You go to file with California. And so even when states have the same basis for exemption like isolated or securities manual they can add further conditions.

So when we at CrowdCheck fear an issue of secondary trading, in addition to getting an audit we need to assure that for some states, there's four of them, that the first closing of the class of securities to be sold was at least 90 days ago, that the class of security has been outstanding for 180 days -- that's one state -- that the issuer isn't in bankruptcy or receivership, that it's been in business for three years or have total assets of 2 million, in some states that it has been in business for at least five years, that's one state, and then another state can impose this unless you talk to them directly that the issuer isn't subject to a stop order, and there's been no major reorganization in the last 30 days.

So you see there is this huge patchwork, and we've discussed it before. I'm not going to get into whether this is a good thing at the moment. I'm just describing how this whole thing works. But the end result is that it becomes very difficult to trade smaller companies, so the bigger companies with institutional investors for the unicorns it's not such a problem. But for teeny weeny companies, and that's a phrase I use a lot for the really small companies that I deal with, it doesn't work for them or their shareholders.

There's a practical impact on the company's willingness to use Reg A, which is what Ryan referred to earlier, and the investor's willingness to invest. What would the solutions be? Well, some people, Joe works with them, lobbying state by state to get the states. Go directly to the states and say please adopt these exemptions. We are seeing in Congress Jobs Act 4.0, for example, proposes a preemption for those Reg A and Reg CF. Virginia has a new exemption for trading on the ATSs focusing on the intermediary not on the nature of the issuer.

I would flag from my own practical experience that when you do not distinguish Reg A and Reg CF you are going to run into problems. There is a huge disparity both in terms of quality of information and compliance with filing regulations between the two.

Anyone who knows me knows I am a huge fan of Regulation A, would like to use it for smaller reporting teeny weeny companies at the SEC level. That obviously does not apply to Reg CF. There is a qualitative difference between the two.

That's all of the boring legal stuff, and of course there will be a test later, but from my own personal commentary I just wanted to throw one thing out with respect to some of the points that Andrea had made which is a possible positive practical impact is with respect to the valuations in the Reg A field. As we know, so many of the companies who raise funds under Regulation A have done so on what we should call optimistic valuations. You may use other terms for them.

What we've seen again and again is when a company up-lists from a nonreporting, nontrading environment up to Nasdaq we've seen that if there was an OTC stock price it goes boom, and we also see this very high volatility when companies first go from a completely private nontraded environment to a traded environment where there's this kind of boop as everybody dives in and then down again. We've seen that happen a lot.

If you had the ability to trade before that, is it not possible that the market discipline may have suppressed the price so that you wouldn't get the ridiculous valuations at least in follow on offerings? Just throwing that out as a possible -- a possible upside of having trading. And then finally, I did want to flag the issue that Ryan had raised with respect to the clunky transfer provisions for getting private shares onto the books -- into DTC, the clearing system, and getting them onto the book of the broker/dealer so that you could hold your shares in your own brokerage account. Anything that could be done to improve that process would be brilliant. Okay. I did the boring bit. Carla, over to you.

MS. GARRETT: Thank you. Thank you, Sara. I really appreciate that kind of overview and background information. I see that Catherine had a question for you.

MS. MOTT: Thanks Carla. Actually, this is for Andrea and everybody here today. As we pursue this discussion, Sara, you said we need to distinguish between A and Reg CF. We also need to distinguish loss and fraud. I heard the word “loss” several times, Andrea, but there's a difference between loss and fraud especially in this asset class. We expect it. That's why we diversify our portfolio. So as we go through this I just wanted to request that we discern the difference between loss and fraud. Thank you.

MS. GARRETT: Okay. Thank you, Catherine, for mentioning that. Sue is going to speak now. She is CEO of a smaller public company. One of the solutions that people also think about is that for the liquidity issues is that the company should just go public, and in Ryan's presentation pointed out a couple of companies that had gone public (audio drop) liquidity. So Sue, would be interested to hear from you as the CEO of a smaller public company about whether there are liquidity challenges for investors in small public companies also.

MS. WASHER: Thank you, Carla, for the opportunity to speak. I alluded to this earlier in my comments, but I do run a publicly-traded on the Nasdaq biotechnology company that kind of went the traditional path for a biotech company in that we raised some seed funding. We went the traditional venture capital route, raised several rounds of venture capital and then went public in 2014, rapidly raised a follow-on and have done several follow-ons since then.

When it comes to the public markets, I do think it is important -- and this is what Carla asked me to speak to. I do think it's important to understand that it's not the solution to the liquidity issues for

Reg A and crowdfunded companies because there are some of the same liquidity issues for small companies on the public markets. If you're a small company, if you're under a certain market cap, it's very hard to get the attention of investors, the big traditional public markets investors.

If you're under 200 million, some investors won't even talk to you. They won't even -- they don't have the time, the bandwidth they feel to pay attention to companies with a small market cap. It's also challenging to raise follow-ons if you're a smaller company because there are constraints on what percentage of your total market cap that you can raise, and there are also constraints when investors think about if I want to fund this company with this amount of money what is the time frame over which I might be able to divest myself from that investment?

Where is the liquidity point? Because for biotech companies I feel as though follow-ons are not liquidity events. They're financing events. The other method that many small companies use and big companies as well but many companies in the public markets use to raise money in between financings is the ATM, or the At The Market, vehicle. Again, if your liquidity -- if your trading volume is low, it is very difficult to make use of an ATM to make use of an ATM to raise any kind of substantial money.

So if the company is still going to be a small company, I just wanted to kind of get it on the record that just going public, being on the Nasdaq is not going to provide necessarily that liquidity that you're looking for, and that's especially true in any kind of company that has a long time frame for development, testing, through any kind of regulatory hurdles before they become commercial and especially now when the capital markets are not working for biotechnology and many high tech companies.

There's been story after story in the last six to nine months where companies have announced positive events, and their market cap has actually gone down due to an issue with shorts, and that's something that small companies and specifically biotech companies have addressed a lot what we feel is a necessity to have more transparency on the short markets because of that kind of problem going forward.

I've already mentioned that the other avenue for capital raising that helps to create liquidity is strategic partnerships, mergers, acquisitions, and with all of the recent discussions from the new FTC commissioner about being pretty much against mergers and acquisitions then that even further constrains an investor's desire to invest in the market because they can't see that as a potential exit which is very important.

So I just wanted to raise some of the constraints that still exist for small companies even when we're on the publicly-traded exchanges.

MS. GARRETT: Thank you, Sue. Appreciate that. And I wanted to see now if people have questions for anyone but especially for Joan or Ryan before just the Committee deliberate on this. If you do, if you could put it in chat or raise your hand or just speak up. Greg.

MR. YADLEY: Thank you all, all of our guests. This is has been a really important discussion, and clearly there are no easy answers. One of the things maybe, Ryan, you could address this. In the offerings that you talked about that ended up after successful rounds with 8,000, 9,000 investors, you also noted the infrastructure mechanical impediments. Could you just go a level deeper on how did that really affect those companies? Were people able to trade notwithstanding, or was it sort of at exit that everybody got those returns that you referenced?

MR. FEIT: Yeah. Sure, Greg. So I guess the first example which I think was the one you were asking about, which is NowRX, they raised their last round a few months ago for us. So all the investors in that company have not had any liquidity, and the anticipation is that there will be liquidity once they ultimately go public or get acquired, the former probably being more likely.

But once you get to a certain size and have that many investors they sort of are forced to have to find that liquidity option, and if there were, I guess, an alternative trading system that existed that actually serviced companies like this particular issuer, I think that would be interesting. But today probably their realistic options are going OTC or going Nasdaq or going New York Stock Exchange at some point unless they get acquired.

MR. YADLEY: Could I ask a follow-up, Carla? One of the things when crowdfunding was still an idea that was viewed as a potential issue was this number of investors, and as companies -- as the ones you've referenced have become more successful and had successive rounds one of the thoughts was that maybe investors might come in and take out those hundreds or, in some of those cases, thousands of investors. Have you seen any of that, or really has it simply been incremental, and as the company grows people feel a little more comfortable that eventually there will be an exit?

MR. YADLEY: I can say that on our platform we've only seen cases where investors have gotten taken out because they've opted to submit to a tender offer which was attractive to them. We haven't seen any of those ugly cases that people have been concerned about with people just sort of like getting crammed down, if you will. I will say that -- I mentioned this before -- every platform has different ways that they treat these offerings, and there have been in the past -- I'm not actually sure if it's still going on, but there have been in the past other platforms that do not have the same investor protections that we have.

And there are either cases where it's happened or it could happen where a sophisticated institutional investor could come in and basically -- sometimes I've seen buyout provisions where you can buy somebody out. I think that could be a negative consequence. You have to have in your legal docs certain investor protections to ensure that doesn't happen.

MS. GARRETT: Bert, I see you have a question.

MR. FOX: Yes. I've been listening to this with a lot of interest as not only someone who sees companies raising capital but someone who gets solicited quite a bit for accredited investor funds, and everything else. I guess my question to either one of the speakers is -- understand the issue, and I really actually do like the idea of having funds for retail investors, but wouldn't there be a role for some level of regulation whether either if it's FINRA, something, right?

Because I can tell you as someone who gets solicited all the time for various accredited investments it's really hard for me to do my own due diligence and understand, you know, what vehicles are on the up and up or not. And so I was very sympathetic to the remarks from the securities regulator here about, you know, again not to protect me from a loss, but how do I know, you know, who's really acting in my best interests versus just a huckster fraudster?

So I guess I'd be really curious in the two speakers' views on, you know, isn't there a role for some level of regulation of credentialing, something like that, without it actually necessarily having to go to all 50 states and have 50 different jurisdictions, and everything else.

MR. FEIT: Yeah. I can take that. And Joan, feel free to hop in after me. But I think absolutely.

So the suggestion that I was making is actually piggyback on Regulation A+ to allow venture funds that are available to retail investors, and by utilizing Regulation A+ you have a significant upfront and ongoing reporting requirement which far exceeds any venture fund that's offered under Reg D, 3(c)(1) or 3(c)(7). So in that case, retail investors would actually have a much higher bar to comply with to provide information to potential investors.

So I do think that if we're going beyond qualified purchasers and accredited investors there should be more information that is required to be disclosed for nonaccredited investors.

MS. ADLER: One of the things, though, when you talk about venture funds and other things, I mean, the barrier to entry to those is usually again you need to be an accredited investor. We come back to the original premise which is that many of the investors in these Reg A offerings and the Reg Crowdfunding offerings are unaccredited investors, not all of them but a significant portion of them, and they don't have the sophistication.

So you have to balance their needs for information and understanding the information that's available so you've got access and digestion of the information balanced against the issuer's needs and the investor's needs on how expensive is it to comply with this. So to Andrea's point, I mean, I work in the Blue Sky realm, the states have sincere interests in protecting their investors, but as Catherine said, you know, there is a difference between loss versus fraud.

So there's a famous example of a Reg D offering by Apple back in the day, and the state of Massachusetts didn't want the private offering to be conducted in their state. And so no one got into certain very early realms of Apple because the states were protecting their investors. Well, they protected them against not making potentially a lot of money. But there are a lot of other companies that are not Apple. In fact, the vast majority of companies are not Apple. Those are the unicorns.

So the question is how do we balance the interests of protecting the investors, which is every practitioner's interest, every broker's interest, the state, the SEC. Everybody is aligned in that. Nobody wants investors to be defrauded, but they do need some avenue, and this is where -- and I know this is a hot button word, but the preemption is not so much that you want to shut down the voices that want to help, but you need to have some kind of uniformity and facility to comply with providing the information.

So that's where perhaps the tension working with the states, and so forth, is what is the happy medium between getting the information out? And then this also kind of reverts back to Ryan's point which Bart was looking at or perhaps it was Greg regarding how do we solve how cumbersome it is for retail brokers to help their customers to get into or out of these securities. They have to deal with suitability, which is a major issue and a sincere concern, Reg D(i) and, you know, and their own internal compliance like Ryan's SeedInvest has, as he noted, a certain internal compliance threshold.

We work with a variety of broker/dealers, and they do run across a spectrum of is there compliance just to what the letter of the law is, or many of them, you know, will go beyond the letter of the law in their policies. There's certainly room for conversation in balancing these competing interests, but at the end of the day the focus does have to be on helping some of these smaller investors. The institutions can speak for themselves, and they often do, but the unaccredited audience doesn't even know that there's a problem.

They would be -- if you spoke one-on-one to Reg Crowdfunding investors, I'm sure they'd say, “Well, it was great to get in, but how do I now sell this thing?" And that's the audience that we kind of need to maybe take testimony from in terms of what might work for them as well as our own interests and what we think is a baseline amount of information that they should receive.

MR. FEIT: I just want to add one quick additional comment to this point, which is one of the -- this was an issue with Reg CF before was amended to raise the cap to 5 million. One of the issues in general for nonaccredited investors in sort of the Jobs Act is that there's a balancing act where if the costs and complexity for an issuer to comply with these regulations is too high then you do have a lemon issue where it's not the best companies that use these exemptions, and in turn that hurts retail investors because they don't get access to the best possible opportunities.

So I think the absolutely best investor protection you can provide is providing a mechanism so that retail investors can get into the best possible opportunities just like institutional investors or accredited investors. That's why a fund is interesting because for most companies if you have access to a fund they could just write you one check. That's a lot more interesting, and so that's why if you'd get nonaccredited investors into these funds directly I think it provides better opportunities ultimately, which is investor protection.

MS. GARRETT: Thank you. I have a question, and it really goes probably to Joan and maybe Andrea. But with respect to the states manual exemption and how that works, I'm sure you guys are much more familiar with this, but it sounds like there's information that has to be provided that would be consistent for that exemption among certain states that have adopted it. And what I'm interesting in is, you know, is that an outdated exemption given that there's not really manual any longer as much there used to be?

And how does the information compare to the information that either would be provided by let's just say a Reg A company that's in compliance with their reporting requirements and the way that the Reg A company provide that information to investors? So Joan, do you want to address that first?

MS. ADLER: Sure. Well, the manual exemption, and this kind of doubles back on what Sara was talking about, if you're an exchange-traded company, you, basically, have the get out of jail free card. You can do your initial sales. You don't have to worry about the states. You can do the secondary trading. You don't have to worry about the states.

When you get to the OTC markets, and we're talking specifically -- because the bulletin board no longer exists, we're talking about the various tiers of OTC QX, OTC QB, OTC pinks. OTC markets themselves created their own manual and, basically, lobbied the states for recognition of their manual because there was only one man standing, which was Mergent. And so that was predicated -- the manual exception was predicated in part on there being public reporting information historically under the '34 Act.

So you had 10-Ks, 10-Qs, 8-Ks with current reporting, and so the manual exemption kind of brought it all together. The manual exemption sat on top of the public reporting regime of what was required, and it, basically, said, you know, if you have your information available in a recognized securities manual then you can have not just -- we're not talking about the unsolicited transactions or, you know, private off-market transactions which still have to be compliant -- they're isolated, as Sara also mentioned, the isolated non-issuer exemption.

You need it -- it served primarily so that brokers could come in and create some liquidity between

-- on a non-deal basis. So you have Company X, like Susan's company. Trading is -- and you want to kind of enhance the market because that's puts you in a better place to raise money in the future, and so forth. So brokers can't recommend unless they have certain exemptions. So the manual exemption helped with whether it's an unsolicited transaction or, you know, certain research reports, certain recommendations, other things. We've facilitated that.

But because of now the Reg A companies and the Reg CF companies you have quasi-public. So they're not reporting companies. They're not putting out the information on a regular basis. Reg A, obviously, as Sara noted, materially different in terms of their continuing reporting than Reg Crowdfunding, but you need to have some baseline public information.

When we put together -- and again my firm has an interest in this, in this GUARDD report, and it's G-U-A-R-D-D. We require an annual audit in order to publish your report, and it's published through the AICPA reporting mechanism so that the companies can't touch the information that goes to the public domain.

You need to have some kind of a venue, and again tying back to the public reporting when you make a public report, if you're doing -- you know, if you're putting out information that is inaccurate, incomplete, misleading, and so forth, you have Section 10(b) issues. You need the same kind of protection in any alternate reporting regime and public disclosure regime.

But we're also finding that companies -- private companies used to be historically very reluctant to put out public information, but because of the whole crowd finance revolution, if you will, they've gotten a lot more comfortable with publishing company information. And so I find that they're more willing to publish, you know, continuing private information so that they can access investors whether it's their historic investors or potential future investors. I don't know if that helps.

MS. GARRETT: Yes. Thank you, Joan. I think before maybe I turn this over to Andrea to answer the question we only have ten minutes left in our meeting today. So I wanted to see if there were any other questions for Joan or Ryan before we say thank you and excuse them so that the Committee can talk among ourselves. Anybody else have any questions for them?

If not, then Joan and Ryan, thank you so much for your time today and for your very interesting presentations and insights into this meaningful topic, and we appreciate that you joined us today. Thank you very much.

MR. FEIT: Thanks again for having us.

MS. ADLER: Thank you.

MS. HANKS: Thank you very much. We appreciate it.

MS. GARRETT: And now that it's just the Committee, Andrea, I don't know if you wanted to address the question that I raised or if you thought that Joan had answered it adequately.

MS. SEIDT: I think she gave a very more detailed answer than I could probably even give.

MS. GARRETT: Okay.

MS. SEIDT: I would say that the manual exemption, as Sara said, is in need of state uniform for it to be effective, and so you do have states recognize OTC first, and then there were some very low-quality deals listing and bad experiences that were listed on that manual which has chilled state interest unfortunately for Joan's firm and some of the follow-up manuals that are being out there.

But I think the issue is making sure investors have the information that they need, and even in the Reg A financial reporting space there's no pricing information. It's hard to value these offerings until investors know what's a fair price, what the real risk of loss may be for them down the road just because we have no data. So thank you.

WRAP-UP AND ADJOURNMENT

MS. GARRETT: Thanks. And just now that it's the Committee just speaking among ourselves, are there points that people wanted to make based on the conversation today? Do people feel that we've come to any type of thoughts on any type of recommendation that this Committee might want to entertain for the Commission to vote on? Yes, Greg.

MR. YADLEY: I think this was really a good day. Sara, thank you for reminding me how complex all of this is. One of the things that I think that Sara said which Carla started out with is it really is a patchwork. Part of that is with deference to Andrea and her colleagues we have 50 states and D.C. and other jurisdictions, and every jurisdiction has a responsibility to protect investors. But as Catherine said, there's a difference between loss and fraud, and I think Regulation A+ has proven to be more resilient than some people including me thought.

I haven't had a great deal of experience with Reg A+, but people are using it. There is a regulatory overlay to it, and it seems to be working in terms of the primary transactions. As was pointed out now you have investors in this quasi-public vehicle, but there's no liquidity, and it is the lack of uniformity among the states that is an impediment. Not purposefully. It's just you got a lot of cooks in the kitchen.

So I think the preemption idea from state regulation for secondary trading for Tier 2 offerings for companies that are compliant with their reporting obligations does in a sense create that uniformity. It may not be perfect to begin with, but there are things we can do. Disclosure is the most important thing that the SEC does in my view in terms of capital-raising, and we can have whatever disclosure people think we need.

The other thing is I don't know if this might be something that if we were to implement this or recommend this perhaps it could be as sort of a pilot program so that people know that we're watching, everybody's watching, the Commission's watching. People will do their best to try and make it work, and if it doesn't work then we abandon it. But we've been talking for a long time. The prior committee that Catherine and Sara and I served on talked about this five years ago. And there have been lots of offerings, but there hasn't been much change in the secondary market.

So I would be in favor of at least on a pilot basis providing friction for Tier 2 secondary trading and Reg A Tier 2 compliant issuer offerings.

MS. GARRETT: Thank you, Greg. Are there other people that would like to weigh in on that? Sara?

MS. HANKS: Yeah. I would certainly agree with Greg. If anything like this were to be adopted, first it should be on a pilot program. One of the reasons why I think Reg A is good is that those filings are reviewed by the SEC. Any preemption should be conditioned on that the company is actually reviewed, that it hasn’t received a no review which I know we've received a lot of those recently. You want there to have been an active review, full review, not partial review, by the staff as a condition to any kind of preemption.

And I would -- sorry, Andrea. I mean, I would be in favor of compliant reviewed companies being preempted to the extent there is statutory authority for it which I would like to see what that actually would be especially in light of what happened in 2020. But in those circumstances, I would like to see a pilot program for preemption of that kind.

MS. GARRETT: Okay. Thank you, Sara. We are coming down to the end of our time. I'm not seeing other hands. I'm going to --

MS. SEIDT: I have my hand up. I would like to respond.

MS. GARRETT: Oh, I'm so sorry, Andrea. I didn't see your hand.

MS. SEIDT: It's okay. I just would like to have one more opportunity to respond to a couple of the final conclusion thoughts. One is we're saying that Reg A is working and that Reg A is a success, and I'm not questioning whether that's true. I do question that there's data to support it. We don't know. You cannot tell me how many Reg A deals have succeeded, how many have failed, how much investors have made on these deals and how much they have lost. You can't tell me that. You don't know that about the primary offering.

So to make a blanket statement that you know that it's all good, and it's great is just a blind statement because you do not have -- we do not have the data to support it. And so you need to be honest about that while you're voting because that's -- and I don't think Sara is going to disagree with me that's the truth. That's the reality. No data. So I really think you should defer a vote in consideration until you have that data. Otherwise, you're really not looking out for investors the way that you are claiming.

And then as to Sara's recommendation for full review, I would just direct your attention to a recent

Massachusetts state order involving a fully reviewed Reg A offering named re Alpha, and notwithstanding a full Commission review Massachusetts was able to find out that the company was posting fictitious property or addresses and pictures of mansions on its application to solicit investment. They weren't real. They had fields that were being portrayed as mansions on their application.

And notwithstanding a full qualification review it was a state securities regulator who identified that investor risk. So I think you need more data before you start walking down this path. I think again states and NASAA are willing to partner with this committee and leaders in this committee to find ways to again make it a safe secondary market for these offerings. Thank you.

MS. GARRETT: Thank you, Andrea. Well, since two people have proposed that we take a vote, we'll go ahead and take a vote. One person has obviously said not in favor of it. So people can vote in favor or not in favor. But it would be the recommendation are we in favor of recommending to the Commission that on a pilot program we support preemption from state regulation for secondary trading in securities of Tier 2, Regulation A securities that are current in their ongoing reports and where the company did not receive a no review. Did I state that correctly? Yes, Sara.

MS. HANKS: Can we throw in statutory authority, providing that statutory authority can be established?

MS. GARRETT: Yes. Okay. Anyone else? And there's a lot of people not on video right now, but if it's possible to turn on your videos while we take a vote.

So for the Committee members that are in favor of that proposal, can you please raise your hand. And Bert and Donnel, I see that you're not on video.

Okay. Let's do a vote for the people that are not in favor of that proposal. Andrea, do you want to raise your hand for not in favor?

MS. SEIDT: I'm a nonvoting member.

MS. GARRETT: Got it. Thank you.

MS. SEIDT: Wish I could.

MS. GARRETT: Okay.

MS. SEIDT: Looks like Bert's in the chat. He can't -- he had to move to his phone.

MS. GARRETT: Okay. So Bert --

MS. SEIDT: He chatted in that he's not in favor if you were to look at the chat.

MS. GARRETT: Yes. He's not in favor of the proposal. It's too specific for him at this point. Is there anybody else? Julie, how did that play out with respect to the number of people that voted in favor?

MS. DAVIS: I'm trying to see. We have eight in favor and one opposed.

MS. GARRETT: Oh, and Donnel says he's in favor.

MS. DAVIS: Okay. Nine in favor.

MS. GARRETT: And is that a quorum?

MS. DAVIS: Yes.

MS. GARRETT: It is. Okay. Well, that means that the recommendation did pass, and we can put that together in a better format that gets distributed to the Committee. I really appreciate the interesting discussion today, and I think we touched on a lot of very important issues. Just so we know our next meeting is on Thursday, October 13th, and we will discuss whether or not there's any possibility of being able to meet in person or not.

Once again I thank everybody's participation on this Committee, and I look forward to talking to you soon. And with that I adjourn the meeting.

(Whereupon, at 1:04 p.m., the meeting was adjourned.)

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PROOFREADER'S CERTIFICATE

In the Matter of: SMALL BUSINESS ADVISORY COMMITTEE MEETING

Date: Tuesday, August 2, 2022

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.

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I, Peter Shonerd, reporter, hereby certify that the foregoing transcript is a complete, true and accurate transcript of the testimony indicated, held on 8/2/22, at Washington, D.C., in the matter of:
SMALL BUSINESS ADVISORY COMMITTEE.

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

8-9-2022