UNITED STATES SECURITIES AND EXCHANGE COMMISSION

SMALL BUSINESS

CAPITAL FORMATION ADVISORY COMMITTEE

Conducted Remotely via Webex

Monday, September 27, 2021

10:00 a.m.

Securities and Exchange Commission

100 F Street NE

Washington, D.C.

PARTICIPANTS:

GARY GENSLER, SEC Chairman
HESTER M. PEIRCE, SEC Commissioner
ELAD L. ROISMAN, SEC Commissioner
ALLISON HERREN LEE, SEC Commissioner
CARLA GARRETT
JEFFREY M. SOLOMON
GREGORY YADLEY
YOUNGRO LEE
KESHA CASH
ROBERT FOX
SARA HANKS
BRIAN LEVEY
SAPNA MEHTA
MARTHA LEGG MILLER
CATHERINE MOTT
JASON SEATS
MARC OORLOFF SHARMA
HANK TORBERT

PARTICIPANTS(CONT.):

SUE WASHER
JULIE DAVIS
JENNY RIEGEL
ANDREA SEIDT

PANELISTS:
DYLAN COX
DAVID NI
PHYLLIS NEWHOUSE
MICHAEL KLAUSNER
ISABELLE FREIDHEIM

C O N T E N T S

P R O C E E D I N G S

MS. GARRETT: Good morning and welcome to today's meeting of SEC Small Business Capital Formation Advisory Committee. It's good to see all of you, albeit, it would be nicer to see you all in person.

Julie, do we have a quorum for the meeting?

MS. DAVIS: We do have a quorum and I'll take this opportunity to just quickly say that any views that the SEC and staff express today are our own views and not necessarily the views of our Commissioners.

MS. GARRETT: Thank you, Julie.

Before we get started, we extend a special thank you to the Chair and the Commissioners for attending today's meeting. You should know that Martha Miller and her great team at the Office of the Advocate for Small Business Capital Formation, do an incredible job at advocating for small businesses and today's agenda is no exception.

It is an honor for all of us to be in a position to help advise the SEC on ways to improve capital formation for small companies, which are an important element to promoting job growth and economic development in the United States.

We also want to thank our guest presenters and panelists today for taking out -- time out of your busy schedules to come to talk to us about two very interesting topics on the ways that smaller private companies are gaining access to public market capital.

We also appreciate members of the public who have tuned in to watch or listen via webcast on sec.gov., and I'm also pleased to welcome a new member to the Committee.

Andrea Seidt, the Ohio State Securities Commissioner and the Chair of Nassau's Corporation Finance Section Committee, has joined the Committee. She replaces Mike Pieciak as NASAA's representative on the Committee.

We appreciate Mike's service on the Committee and we are pleased to welcome Andrea to the Committee.

Jeff, would you like to take over?

MR. SOLOMON: Sure. Thanks, Carla.

And, throughout the COVID pandemic,

our Committee has really shared with the Commission observations on what small businesses are experiencing in various industries and locations, and today we will continue that dialogue by sharing our latest perspectives on interesting trends and changing dynamics in our areas of the market and how access to capital is impacted.

While the primary purview of the Committee has been to focus on ways to improve access to capital for companies that are generally under 250 million dollars in value, we're going to be learning today a little bit more about how companies in that range can access public market investors as they continue to grow larger.

The health of the public market investors and publicly traded companies play - plays an important role in ensuring that smaller private companies continue to thrive. While many smaller private companies may not ultimately avail themselves of public markets, when the public markers are working well for investors in small capitalization companies, capital continues to flow to smaller private companies, particularly the ones that require significant capital to grow.

Following the member updates, our discussion will focus on two important innovations in public market capital raising that have become much more important to the revitalization of public listings that has occurred over the past decade since the passage of the Jobs Act by Congress in 2012.

The Committee will spend this morning learning about the dynamics of crossover financing from the head of PitchBook's private market research. Generally speaking, crossover financings occur as a last round of private financing before a public company accesses the public markets. PitchBook's recent report shows that nearly 75 percent of IPOs, by count, has received -- had received late stage investment from nontraditional venture investors.

These so-called crossover investors are typically public equity investment managers, such as hedge funds, mutual funds, and pension funds that are crossing over to incorporate more private into their investment strategies. It is a convention that is gaining traction, in part, because it enables a group of public market institutional investors, like mutual funds and the like, to spend considerable time with companies and make meaningful investments in them before they are public.

Ultimately, many of these companies will cross over. Many of these crossover investors become anchor investors in a company's IPO and become significant long-term shareholders. Some of the data you will see and hear about today demonstrates the companies who compete -- who complete crossover financings before going public have much better experiences in their early days as public companies than ones who do not.

It should also be noted that crossover investors, while institutional in nature, are a way for smaller investors to participate in capital formation since oftentimes the investors in mutual funds and pension funds are comprised of individuals.

The Committee will also explore how this trend is leading to higher valuations and why crossover investors have become ubiquitous through the cap tables of VC-backed companies that ultimately --

After the lunch break, we will be learning about innovations in public offerings that have also occurred, and while our Committee is focused on capital formation pathways for small public companies, it's important to evaluate the pathways for private companies that enter the public markets, and we will explore the differences between a traditional IPO and alternative paths, including direct listings in SPAC mergers, all of which are ways for private companies to access public capital.

Direct listings and SPACs are not new market conventions; they've been around for decades, but over the past few years, there has been an increase in utilization of these alternatives by private companies as a way to get public. Each of these paths to accessing capital are different and they all have pros and cons for both companies and investors.

In other words, when small private companies consider various paths to choose, one size does not fit all. While having choices to consider can lead to better outcomes, that is not a certainty, and there are clearly improvements that can be and should be made in each path in order to increase the likelihood of better outcomes for both companies and investors.

With that in mind, we have lined up a great panel who share the benefits and risks associated with each of these paths for companies and investors, and we'll also hear thoughts and suggestions from panelists on ways to improve experiences and outcome for various constituents in the equity capital formation ecosystem.

We understand the Commission may propose rulemakings that refine pathways to going public, including via SPACs, and our discussion today will help illuminate those future rulemaking deliberations. Hopefully, the insights we can glean from our panel of experts will enable us to have a robust discussion and perhaps even make recommendations to the staff that will enable them to make tangible improvements in the way companies access capital while maintaining and enhancing the essential elements of safety, soundness, and investor protection.

Carla.

MS. GARRETT: Thank you, Jeff. I think it's going to be an interesting day today, so -- but before we get started, we'd like to welcome Chair Gensler and the Commissioners who are with us and we would -- I'd like for you to make any opening remarks that you'd be interested in making.

Chair Gensler.

MR. GENSLER: Thank you, Carla. Thank you, Jeff, for that review. It's good to be with the Committee again and I'd like to thank the members for their time and willingness to represent the interests of America's small business, and as was said, and it's customary noting, that I'm speaking on my -- on my own behalf, not on the commission of the SEC.

I look forward to the readouts from today's discussion. Late stage private rounds of financing -- so-called crossover investing, as Jeff just went through -- as well as pathways into the public markets.

Last time we gathered, I spoke a little bit about my dad, Sam Gensler, who was a small business owner. I mean, it was never more than a few dozen people. He didn't access the broad capital markets as we're discussing today. He would've marveled at these dollar amounts. That wasn't his business.

But as a society, I just want to say, the U.S. is really blessed with the largest, most sophisticated, most innovative capital markets in the world, and our companies, including small businesses, rely on our capital markets more than companies in any other countries. I mean, we really have this and consider this:

Our U.S. capital markets are about 38 percent of the world's capital markets. That compares to just 23 or 4 percent of the world's economy, so you can see how that's outsized, or another statistic, that our corporate bond market alone is about 10 trillion and that's about the same amount of lending in the entire commercial banking sector to -- not just corporate, but to non-corporates and individuals. So, our capital markets are really pretty significant to this equation.

Broadly speaking, as small businesses grow -- grow beyond Sam Gensler's business -- but grow, they often migrate from borrowing in bank markets to borrowing in capital markets, and sooner in our markets. And they also, as Jeff laid out, start to consider tapping into the equity markets as well, and having that breadth and depth in our markets facilitates capital formation. That's why we want to make them the most efficient that we can.

Now, I just want to say a few things about SPACs that you're going to talk about; I'm going to listen closely and hear the reports on the crossover investments.

This year, there has been an unprecedented serge in the Special Purpose Acquisition Companies, SPACs, which has provided an alternative an alternative to traditional initial public offerings, and as Jeff said, also a few -- just a handful of direct listings as well.

As technology and markets evolve to challenge existing business models, I think it's important to think about how we, not only protect investors, but also facilitate the capital formation, and with SPACs, there are a lot of costs in between the companies that are raising money and the investors on the other side, and -- is not about capital facilitation, and formation, and investors, but the fair orderly and efficient markets in between.

SPACs are shell companies that raise cash from the public through, what I would call, "blank check IPOs". They generally have two years to then find and merge with a target company and that sets up the target IPO, that which you all will be talking about later today.

We can see the SPAC sponsors generally receive about 20 percent of shares upfront, but only if there's actually a deal later. The first stage investors get redeem when they find the target, leaving the non-redeeming investors and later investors to bear the brunt of that dilution.

So, if you're a small company thinking about merging with a SPAC, the promoters are taking about one out of five shares -- 20 percent -- and then in addition, there's other costs as well. Once they find a target company, the SPACs also often raise money through transactions known as private investments in public equity, PIPEs. This Committee, of course, knows that; you'll be talking about it later.

These deals give the new investors, mostly big institutions, an opportunity to put money into that target IPO, but these PIPE investors often buy shares at a bit of a discount to what the share price will be after the target IPO. They're bearing a few extra days' risk; they're doing some due diligence going in, but they receive some benefits along the way. The result, PIPE investors often get a better deal than the retail investors.

There are a lot of costs in these structures, and these structures, whether they're the sponsor fees, the 20 percent fees dilution potentially from the PIPE investors, fees to the various advisors along the way, these costs are born by the companies trying to access the markets and by the investors. In essence, more costs in the middle; that means the investors and the companies are bearing some cost, and it may be that those fees are coming out of the retail public as well.

So, I think for small businesses considering going publicly as SPACs, it's important to consider the cost as well and whether it's the best approach, and that's part of why I've asked staff for recommendations -- to our five member Commission -- to think through how we might update our roles so that investors are better informed about the fees, the costs, potential conflicts that may exist in these structures.

I do think that it's worth considering also what we learn from the SPAC market and the direct listing market, and whether there are changes that might be appropriate for traditional IPOs because they're competing -- these various alternative capital formation and public offering formations are going along.

So, I look forward to hearing, of course, from this Committee, and from the broader public on these topics, and I turn it back to Carla and the team.

MS. GARRETT: Thank you very much, Chair Gensler.

And Commissioner Peirce.

MS. PEIRCE: Thank you, Carla and thanks to the Committee members and today's panelists. Welcome, Andrea. It's particularly nice to have a fellow Ohioan on the Committee. Thanks to Mike for serving on the Committee.

I'm looking forward to today's discussion on small business capital formation trends, at this stage in the pandemic, and the changing dynamics of pre-IPO financing and going public.

Two tends to be featured today, which we already heard something about, are SPACs and the significant increase of institutional investor participation in late stage private capital raising rounds demonstrates a hunger for growth opportunities in today's market. Making it possible for retail investors to get access to some of this early growth remains important matter to the Commission's consideration.

The desire to expand private investment opportunities to more individuals was on full display at our May 2021 Small Business Forum. The Forum's report, which was released this morning, includes valuable policy recommendations by the participants, many of which has been discussed by this Committee. The report includes some frustratingly non-committal responses by the Commission.

History teaches us that the Commission's non-committal responses with regard to Forum recommendations could translate into no action at all. Now is not the time for a full response to all of the Forum's recommendations, but I will address a few of them and urge this Committee to continue pushing the Commission to show more of a commitment to facilitating small business capital formations.

Forum participants recommended that we expand the accredited investor definition to include other measures of sophistication, such as specialized industry knowledge or professional credentials. Another recommendation similarly suggested that we expand the definition to include an investor certification course or test, to show curriculum has been improved by either FINRA or the SEC.

My response is that, ideally, the Commission would get out of the business of telling Americans that they are not rich enough or smart enough to invest their money as they wish, but short of that, the Commission should entertain proposals from the public to expand the accredited investor definition to cover additional certifications, designations, and other credentials.

My preference would be to anointing one institution or entity to design and administer a knowledge-based exam. We might consider, instead, allowing multiple tests or accrediting successful completion of two or more investing related courses at any accredited college or university, but I'm open to other options.

Forum participants also recommended that we revise crowdfunding to remove the gap financial statement requirements from businesses looking to raise a small amount, preemptive State Law for secondary transactions for shares issued under Reg A or Reg

Crowdfunding and establishment a micro-offering exemption. My response is that we need to create workable options and remove regulatory barriers that prevent small businesses from using these options.

Since the beginning of the pandemic, Reg Crowdfunding has emerged as a vital capital formation tool and I'm pleased that the Commission provided temporary relief with respect to the financial statement review requirements in that regulation. The positive feedback from that exercise suggests that we should be open to exploring other tweaks to Reg Crowdfunding, and likewise changes to Reg A, may help to expand its use, and its streamlined micro-offering exemption might be particularly helpful for early stage founders in communities without many deep pockets or easy access to specialized legal help.

Thank you and I look forward to hearing your thoughts and observations as today's agenda focuses on the other end of the spectrum of private companies close to going public.

MS. GARRETT: Thank you, Commissioner

Peirce.

Commissioner Roisman.

MR. ROISMAN: Good morning. Thank you, Carla, and welcome. As is custom, I'll start by saying my remarks this morning are my own and don't necessarily reflect the views of the Commission or my fellow Commissioners.

It's also customary for the Commission to say that they are looking forward to an advisory committee's discussions, but I am especially looking forward to your discussions today. The topics you'll be covering are crucial to our understanding of how smaller businesses are accessing capital, and I'm particularly interested in hearing bother your panelists and your discussions today.

Investment and private offerings has been a hot topic for several years now as the private market has expanded. One of the key concerns that I've had is that there have been few opportunities for retail investors to capture much of the considerable wealth that has been generated by some of our country's most dynamic companies.

It seems, however, that these opportunities have not been entirely missed as data show that pension funds and mutual funds have become active participants in late stage investments in these private companies, along with other types of crossover investors.

I'm pleased that at least there's some of these vehicles. Some every day Americans have been able to tap into the resilient growth in our private markets. Given that they're investing through highly sophisticated fund managers, and these managers are overwhelmingly invested at a point in company's growth where risks have receded, this seems to be a good outcome for those beneficial owners.

Our disclosure rules, and lines we have traditionally drawn between public and private offerings rely on the concept that our mandatory disclosures may not be necessary for an investor sufficiently sophisticated to be able to request, receive, and evaluate the information needed to make an informed investment decision. These investments, by mutual and pension funds, would seem to meet that standard.

Of course, not all retail investors are able to access such opportunities. An individual, non-accredited investor is still not able to invest in private offerings. As I've said frequently in this and other settings, we should continue to evaluate ways to expand the accredited investor definition to allow more individuals to access potentially valuable investments.

Also, not all of the crossover investors represent primarily retail investors. To the extent that the influx of crossover investor funds allow a greater chasm to grown between accredited investors with access to a rich array of investment options, the retail investors who overwhelmingly cannot access these opportunities, this only underscores the fundamental unfairness excluding people of moderate means from the investments with great growth potential.

All this is to say, I hope that this Committee will continue to explore ways that all investors might participate in and benefit from our innovative and dynamic private markets.

I'm also looking forward to your second panel today. As going public has become more challenging, companies have discovered or rediscovered alternative or novel ways to reach that goal. We've recently seen a considerable boom and rapid diminution in the number of SPACs. We've also seen a number of companies opt for the direct listing route.

Here at the SEC, we see the numbers and the headlines, but often miss the stories on the ground. I'm very interested to hear how today's panelists have navigated the various channels toward public listing, what challenges they have faces, and what regulatory changes might affect the markets.

Thank you again to our Committee members and our guests. I look forward to your remarks and discussion, and thank you, Andrea, for joining us, and I really looks forward to your participation and input.

MS. GARRETT: Thank you, Commissioner Roisman.

Commissioner Lee.

MS. LEE: Thank you, Carla and good

morning to the Committee members and the panelists today.

I want to join the others in thanking Mike Pieciak for his service on the Committee and welcoming Andrea Seidt. I'm really grateful to both of you for lending your time and talents, and for perspective that State Regulators bring -- State Securities Regulators.

I'll be brief and let you get to your busy agenda, but I do want to say a few words because both of your panels today implicate a topic that, I think, should be a key area of focus for the Commission, and that is how do we help companies grow and progress toward IPO in a way that protects and preserves the fiber and opportunities that our public markets afford to investors, especially retail investors.

So, in that regard, I look forward to the first panel on pre-IPO financing with an emphasis on the role of so-called "crossover investors".

Now, the backdrop for that discussion is, of course, the growth of capital in the private markets and the expanding length of the time that companies remain in those markets.

So, in this context, where companies can raise huge amounts of capital privately and delay IPO almost indefinitely, it's not surprising that some investors, including those that traditionally invest in public markets, have begun to expand into these pre-IPO rounds in order to try to capture some of the growth opportunities they present.

And the phenomenon raises some important questions, including whether and to what extent what may be valued by investors in private pre-IPO rounds of financing aligns with what public investors expect post-IPO, and whether the data shows that crossover investors can actually help bring a discipline and a focus on pathways to profitability, similarly maybe in some respects to the due diligence that underwriters bring. This is especially relevant to the extent that retail investor interests are at stake for some of these crossover investors like mutual funds.

And then I hope you'll also help us

think through some broader issues related to private companies growing so large and staying so long in the private markets. I'm query whether this is a positive development for average every day investors and the transparency on which our capital markets thrive.

Your next panel topic dovetails with the first in that it continues to explore how we facilitate public investment opportunities, and in that respect, as I've previously said, I'm interested in how recent market developments and innovations, like SPACs and direct listings, have the potential to help issuers address some the challenges involved in going public and, therefore, hopefully enliven public markets and expand investor opportunities.

Of course, we must ensure that the opportunities these innovations present have sufficient protections for investors so that these innovations can retain viability in the long run as a tool for capital formation. So with respect to SPACs, in particular, we've seen more and more of the risks that these transactions present and that's why I'm very glad to see SPACs on the regulatory agenda.

So, I hope you'll help us think through how to ensure that the opportunities associated with SPACs include appropriate guardrails and transparency to protect investors.

For example, how do we ensure that SPAC disclosures provide investors with a sufficient understanding of the target company and its risks and operations, and are there problems stemming from the fact that there's no so-called "quiet period" for these merger transactions, as you would have in an IPO, and how can we ensure that SPAC sponsors and other financial advisors have sufficient incentives to perform robust due diligence.

There are numerous other questions regarding SPACs and direct listings, but I'll stop there and let you get to your work today, and thanks again to all of you for your continued willingness to contribute your time and expertise.

MS. GARRETT: Thank you, Commissioner Lee.

I also wanted to let you know that Commissioner Crenshaw sends her regrets. She is not able to join us this morning, but thank you Chair and Commissioners for your remarks and we look forward to, you know, progressing with the meeting.

As Jeff stated, the next item on our agenda -- or the first item I should say -- is for members of the Committee to -- are invited to share their updates and observations on interesting trends changing dynamics in their area of the market, the impact of forward-looking pandemic preparedness, continued remote work, antidotes to the rise of new business formation, entrepreneurship coming out of the pandemic, or any other items that you would like to share.

Now, we are going to go in alphabetical order by last name and -- so, therefore, Kesha, you get the honor of going first.

MS. CASH: Hi. Good morning.

A couple of things that I'll share -- and I'll be quick cause I have a loud construction noise outside -- but a couple of things I'll share, as an impact investor, some news that's getting us excited, our foundations, particularly the McArthur Foundation, announced last week a greater -- its efforts to create a greater line between its 7, 8 million dollar endowment in its mission and its values under core things, including climate change, diversity, and racial justice.

So, this is exciting as we talk about capital formation. How do we align that capital and the access to capital with mission so that we are having a greater benefit and impact on larger numbers of Americans.

In addition to that, another set of newsworthy mention, Silicon Valley Bank recently purchased Boston Private, and as part of that acquisition, they announced an 11 billion dollar Community Benefits Plan with 4 billion dollars over the next five years being allocated to small businesses and small business loans; another 4 billion allocated to Community Reinvestment Act dollars, which we know is a large pot of capital that can be used to catalyze further innovation in underserved markets.

So, we 're excited on that -- on the impact side to see these larger dollars being aligned, again, with mission and values, which we think is the way to have a greater impact on lower moderate income Americans.

MS. GARRETT: Thank you very, Kesha.

And next on our list is Bert. Welcome.

MR. FOX: Thanks, Carla, and thanks, Commission -- Commissioners.

You know, I would say, observations on this topic, our -- my firm has been exceptionally busy for the last almost year. The amount of capital raising activity is really also phenomenal -- what's going on right now. Yeah, I'd say we have well in excess of 100 -- 100 to 150 clients that are actively trying to seek acquisition via SPAC or traditional, go public route.

You know, to me, I think that there is a -- there's a lot of attraction to a number of the SPAC situations, especially the ones that we're seeing where you have a more sophisticated sponsor.

They actually can bring some additional expertise, similar to a private equity group, to the deal, but it also seems simply that the level of SPACs has really raised the valuation in the marketplace and, you know, we're seeing even a lot of family-owned companies -- ones that even potentially have hundred plus year history as privately held companies -- now seeking to access to capital marks -- lot of cases because, frankly, the valuations are so attractive that it's hard for them to pass up the opportunity.

So, I mean, I think, you know, we are definitely seeing for the first time in a while, the pure number of public clients that we serve is going up, and the amount of capital raising activity is very robust right now and the pipelines are full.

I mean, I know I've talked to multiple attorneys, bankers -- everybody else -- and they're all, essentially, capped out. You know, essential -- they have so many deals going on and, you know, even for us, staffing is quite an issue.

So, I mean, I think it's an exciting time, cause, you know, again, for the first time in a long time, the number of public companies is actually going up in the U.S. You know, I think it is open to the debate.

I think the Commissioners already raised a number of very worthy issues to explore as to whether this is the right set of incentives, and the right structures, and the right level of protections, but I think that -- you know, I look forward to our future discussion, but it is very much a true statement that it's not just the level of SPACs, but the amount of just clients accessing the capital markets is up tremendously.

MS. GARRETT: Thank you.

Next on the list -- so I will share my observations. They'll be a little bit less about public companies and SPACs, as I tend to represent much smaller companies.

I have seen -- and my law firm has seen -- just an amazing amount of deals, a lot of acquisitions, a lot of capital coming into small businesses. We've also seen a lot of new people starting companies. So, again -- which is nice -- and the other thing is that I've seen the companies -- a lot of companies that have gotten PPP loans are now really starting to benefit from those loans -- not that they didn't before -- but now they're starting to not only, you know, take advantage of them, but they're starting to grow again.

I have a family small business, and for us, it was a wonderful bridge during a time that our revenues were very low and, therefore -- since we sell books to schools -- but, therefore, you know, it helped us bridge the gap so that we were able to now start where, even though the pandemic is still going on, it has a lot less effect on our business, and I'm seeing it having a less effect on other companies -- businesses too that I work with.

So, that's my short take on very small companies.

Sara, you have audio?

MS. HANKS: Can you hear me?

MS. GARRETT: Yes.

MS. HANKS: Okay. Fantastic.

Yeah, we thought -- we've experienced in the online capital formation area pretty much the same as everybody else throughout the capital markets; huge amount of growth. We're seeing increases in -- in bases across all of the exemptions -- Reg C -- Reg F, Reg B -- that continues a trajectory that we saw, even prior to the changes in the offering amounts that went into effect in March of this year.

I don't think the increase in the -- in the offering amounts has actually had as much impact as the overall activity. Companies are generally not reaching those increased dollar limits.

In the online area, we're -- we're five years into the Reg C Act; we're six years into Reg A and we're seeing a lot of companies and a lot of investors and we'll see what's next. Is there an exit? And that's actually quite a challenge for early stage companies. The two options really are finding a quotation forum, which is -- which is a challenge. There are a number of new alternative trading systems that are standing up.

The challenge for early stage companies to be quoted on -- in those forums is

-- the challenge largely comes from State Law. There is no State Law preemptions; they all must comply with all trades that take place in those forums and that can be very expensive for early stage companies. The other option is acquisitions.

One thing that we are seeing for these companies is the impact of Rule 145 on early stage acquisitions. If there is a vote with respect to an acquisition, there is an investment decision, and even with respect to numbers and securities, those are very frequently a statutory vote, which means that if anybody gets to make a decision about whether their shares get acquired or not by another company, that transaction must be complied with by the -- rules.

That can be very difficult for smaller acquisition -- smaller companies looking to doing an acquisition, which does make SPACs more attractive that these companies are still very small.

So, we're in challenging times when we're looking at -- the question of what happens next with this investment --

Back to you, Carla.

MS. GARRETT: Thank you, Sara, for that.

Youngro.

MR. LEE: Hello. Good morning.

It has been a very interesting period, to say the obvious, over this year since the -- pandemic is obviously going on -- but there was a lot of actions and definitely the one highlight that I'd like to specify is the new changes of Reg A Crowdfunding and other related Securities Laws back in February, March has, in my opinion, definitely been an overall net positive for the economy.

And what I mean by that specifically is that there are much more companies that are frankly much more sophisticated and advanced, tech savvy, and probably higher quality using, you know, superficial metrics that are interested in utilizing Reg CF and other profiting mechanisms than ever before, and I think that was one of the main goals of this Committee, but also the Commission in the prior years, to basically increase access to both companies looking to utilize these laws, as well as, obviously, investors looking to invest in them.

But when you dig in a little deeper -- I will say that, you know, I also work a lot with -- as Carla mentioned, a lot of small businesses -- and there continues to be a divide between these high-growth tech companies, as well as, you know, I guess, the really local small businesses.

That's -- you know, having been through this -- you know, this Committee for a couple of years now, it -- there's not much that anybody can do, obviously, to change the macro conditions of technology and advancement of technology.

I think that -- you know, everyone -- but I will say that the small businesses continue to struggle and the companies, even at the local business level that are actually, you know, thriving and growing in this new normal, are not necessarily the type of small businesses that I think these -- this Committee and all others think about in terms of what's support in terms of lifestyle business -- mom-and-pops. It is probably the more national or more capitalized, almost, venture capital models that are now trying to tackle small businesses.

So you know, it's neither -- I don't think that's neither good or bad. It's just a reflection of how the world is changing, but the nuances of Securities Laws continue to matter depending on who you're looking at, whether it's the -- of Starbucks or the truly local businesses. Thank you.

MS. GARRETT: Thank you very much, Youngro.

Brian?

MR. LEVEY: Hello. Just some observations from me, and I wanted to highlight some observations of our chief economist, and as a reminder, I work at Upwork, which is a remote work platform for knowledge workers.

So, what we've observed during the pandemic, as far as business formation, entrepreneurship, and remote work trends, obviously, U.S. business registrations surged during the pandemic. While U.S. company payrolls are still millions of jobs below pre-pandemic levels, self-employment has fully recovered and then some, and one driver of this wave of entrepreneurship, our data shows, is coming from these remote work platforms, one of which I work for.

Going forward, we believe, what we call and what we've seen -- being called the "Great Resignation", will bring even more people to remote work platforms in search of remote work and flexibility. Offices are reopening; many are not excited to go back to the office. Remote work has become highly valued for some.

I think there has been -- and what we've seen -- there's much more focus on outputs. You know, is the work getting done as opposed to the inputs, the bodies in the seats in the office, what we've traditionally known; much less focus on face-time in the office, we think, when folks do get back. So, we think it's -- the return the office is fueling some of the "Great Resignation", and as part of that, many are returning to remote work and freelancing. We expect growth in the freelance work force.

And as far as just observations from

the chief economist, remote work forums -- platforms can help increase -- for small business, as well as the talent. Remote freelancing gives these small businesses the tools to focus on their core competencies; it also lowers their overhead costs, and we do believe that remote freelancing is additive to the economy.

So, when we ask clients what they would've done to get the work done had they not hired freelancers or remote workers, the most common answer is "Do the work myself". Only eight percent would've hired more full-time employees to do the work. So, we believe that remote work platforms can be additive to the economy by creating these new opportunities.

So, just some observations from our end and I will pass it on. Thank you.

MS. GARRETT: Thanks, Brian. I would imagine your company has been quite busy in the last year.

Okay. Sapna.

MS. MEHTA: Hello, everyone. Good morning.

As far as I can see, I'm glad we're

talking about the SPAC market today. At Revolution, including our fund, Rise of the Rest, we have seen a lot of our companies go through the SPAC process or are, you know, going through it or in the pipeline.

You know, it is -- it's interesting to see the results, you know, a month after the De-SPAC process, six months after, and a lot of it, I'm just curious to hear everyone's thoughts. But, you know, you can see a lot of the companies going through growing pains of being a public company in the public rather than doing it more behind the scenes in a traditional IPO process.

But we've seen varying degrees of success, you know, for the companies, themselves, and early investors, so I'm really interested to see what people say about that. And in terms of -- I mean, I think we've had the busiest quarter that I can remember this past year. Valuations continue to be very high; we are continuing to find great companies. Our companies are continuing to get funding; it's just a much different landscape than we were in a year ago.

So, that's all I have.

MS. GARRETT: Thank you very much, Sapna.

Martha.

MS. MILLER: Good morning, everyone. Good to see all of your faces. We've got a lot of wonderful things happening with our team, notwithstanding all working remotely and seeing each other tiled across the screen as the new normal for our meetings that has, I think, sunk in for each of us.

As was mentioned earlier this morning, we just delivered the report on the SEC's 40th Annual Small Business Forum to Congress, as well as to subscribers to email updates from our office.

So, I would encourage you to check that out. The entire team put in a lot of work collaborating with the Commissioners, as well as the different rulemaking divisions in preparing that, with a special shout-out to Amy Reischauer on our team, who was the MVP of the Forum, and getting that prepared.

As already has been referenced, we've been hearing updates and trends from a number of different folks that we talk to; interesting reports on increases and people trying to raise capital online and bridge connections outside of their geographic area or personal net worth -- or not -- network, not net worth -- and lots of feedback about recycled capital coming back into the ecosystem as a result of some these exits, which hopefully bodes well for some earlier stage companies that are getting their businesses off the ground and are going to have capital intensive needs, and we continue to be talking to lots of people who are looking at innovative solutions to some of the challenges and how to creatively solve problems where there are gaps in capital raising.

So, we look forward to continuing the work and collaborating both internally and externally with the many wonderful partners we have.

MS. GARRETT: Thank you, Martha, and thank you for all of the work that you and your office do. It is an amazing amount of work and we really appreciate it.

Okay. Catherine.

MS. MOTT: Good morning. Thank you, Carla.

So, just to remind everyone, I focus, where we work, primarily the Midwest, so Pittsburgh over to Sioux City and -- so, what we are continuing to see, consistent, with what everyone else is commenting on, is an increase in the ability to raise capital online, however, it does feed the barbell affect that we see in our market.

It is as -- plenty of seed capital, you know, in that segment of -- you know, of capital is highly -- is growing, I would say, much more quickly, and also we see a great deal of late stage capital. It creates this gap at the point where companies are raising capital, or as they achieve growth, and achieve milestones, and demonstrate that they've built more value in their company and at a point where they need additional equity capital cause they still aren't at a point where they can borrow money from banks.

We're seeing a dearth of capital in that point where it's typically called Series A and is now being called, by the community, the

"Valley of Death", and the '99 Investor Law continues to tie hands of those who could raise funds that could, you know, achieve -- I would say achieve professional management and -- for these funds and provide the capital necessary.

Most of our exits occur by M&A; that's how we've achieved our exits throughout the years, and for us, I mean, the public markets sometimes play into our ability to provide -- you know, to liquidity options and recycle the capital. I think I heard earlier that Martha mentioned that happening; that happens commonly here. Investors will recycle their capital back into supporting new company formation.

So, anyways , that's where we are here in the Midwest. We're -- we have to have access to more mid-stage capital in order to attract the talent from the Boston, New York, and California investors, who are much larger investors and can continue to support the growth of our companies. Thank you.

MS. GARRETT: Thank you, Catherine.

Jason.

MR. SEATS: Hey, everyone. Jason

Seats, Chief Investment Officer at Techstars.
In 2021, we've seen a continuation of all the trends that were pre-existing over the past several years; trends that include increase in total venture dollar flow, increase in round sizes, increases in valuation. The most notable thing to point out about this year though is just how dramatic the trends have extended in the first half of 2021.
Total venture investment dollars deployed are basically twice the amount that happened over the first half of 2020. In VC circles, a pretty common discussion topic today, is just how much valuations have moved, and there are very early stage financings happening for seed stage companies that are pre-launch, pre-product that are receiving pricing that not that many years ago would've only been seen for growth stage companies.
And perhaps relevant for today's discussion, a big driver of this phenomena is the entrance of very large late stage, including crossover public market investors who are now investing not only in pre-IPO companies, but in every stage of venture,

including at the very earliest stages, including seed stage.

So, I heard a story last week of a top tier, well-known Bay area VC losing out to several deals to a well-known hedge fund that invested in these pre-product companies that were pre-launch at an implied valuation of 75 million dollars.

Those of you who participate in C Stage venture understand why the descriptor "crazy" has been used to describe this phenomena, but also worth noting, it's generally accepted that the majority of these dollars are flowing into what you could best characterize as obvious entrepreneurs, and by this I mean entrepreneurs are individuals with pedigree backgrounds -- serial entrepreneurs -- people living in major funding hubs on the coasts, and that means a continued exaggeration of the chasm between the haves and the have notes in venture capital.

Entrepreneurs who are obvious to back are seeing unprecedented demand from investors and entrepreneurs located in the middle of the country, especially underrepresented and underestimated founders, are not seeing the full benefit of this increase in financing or this increase in pricing, and I think in this forum, we should continue to debate the mechanisms about which we can support underestimated entrepreneurs and the investors who fund them.

So, at Techstars, we like to say -- this is a common saying -- but "Talent is distributed evenly but opportunity is not", and, personally, I believe the long-term health of our economy and financial marketplace hinges on our ability to close this fund and gap.

MS. GARRETT: Thank you very much, Jason.

Andrea, welcome to the Committee. We look forward to having you on it and we welcome your thoughts.

MS. SEIDT: Well, I just joined on Friday so I don't have any remarks prepared, but I'm very excited to join and learn about what you're doing.

I have been with Ohio for a long time and have been actively involved with NASAA for a long time, and so you probably won't be surprised to hear that NASAA and the states are very interested in finding ways to better balance capital formation policy with investor protection concerns. You know, we definitely are interested in getting as much data as possible.

A lot of times when I sit in on these things, I hear how much money has raised and what's going into the private markets. States are very interested in seeing what happens with that money in terms of job growth and in terms of investor performance, particularly retail investor performance.

And so thank you for having me. I look forward to learning about of these things today. So, thank you.

MS. GARRETT: Thank you for being part of the Committee.

Marc.

MR. SHARMA: Thank you, Carla. Good morning, everyone. Just a brief update:

As you may know, the SEC Investor Advisory Committee met on September 9th and they issued a number of recommendations on SPACs which I think may be relevant to some of today's discussions, which I'm really looking forward to, and without further ado, I yield my time back to you, Carla. Thank you.

MR. SOLOMON: Carla, you're muted. I assume you were saying me?

MS. GARRETT: Yes, I was telling Marc thank you and thank you for sharing his -- the information with the Committee.

Jeff.

MR. SOLOMON: Right. It's nice to see you. Thanks, everybody, for being here and thanks to the Commissioners and everyone for taking an interest in this.

You know, what we've seen is not just similar, so I won't go back over it, and we've certainly seen a plethora of people needing access to capital, and I honestly think it's situational or environmental, meaning, you know, right after one has a really big scare, like they did during the pandemic, and they realize how important capital can be to executing other business plans, I think just a lot more people -- a lot more companies have decided to try to access public markets because even -- you know, they're sort of valuation sensitive, but not exactly in some instances, because they know if they can get access to permanent capital, or they get access to capital generally in the public market, it gives them an ability to continue to fund their business plans.

You know, where we've seen, we've seen a lot of people clustering in terms of, not just the product type, which would be SPACs or IPOs, but we're seeing it by industry and they're a very capital intensive industries, like ESG industries -- electric vehicles has been a big area -- ag tech has been another big area where we've seen significant growth and I think there's a lot of improvement that has to be made.

Just to give you some stats -- and I feel kind of funny saying this a little bit cause, you know, like Chair Gensler's father, my father is the same way. These numbers are silly number compared to what we grew up with in our household. So, it's just -- it's hard to wrap your head around it.

But when you think about the amount of capital that has been raised just in SPACs, just for ESG companies, since Nicola went public through a SPAC in June of 2020, it's 230 billion dollars. That's just for ESG related companies that are transforming, you know, old -- what I would call old economy businesses like trucking, and transportation, and work force automation, and agricultural technology.

Along with that comes a lot of job growth too and I think for a number of the companies that we've seen that have raised the money, they've doubled, tripled, quadrupled their head counts in areas that don't generally get funding, and I know on this group we've talked a lot about some of things we've done in western Kentucky, but also Upstate, New York. You know, when these companies do get access to capital, they do hire people, and that's an important part of it.

Having said all that, there has been excess and I think it would be -- you know, we would be remiss if we didn't address some of the real issues, particularly some of the recommendations coming from -- Marc, from your Committee, which will go to providing investors with much more transparency than what's actually happening here and I think that will be really helpful.

I also note that we've been pushing in our -- you know, as a firm, we've been pushing a lot for what Commissioner Peirce said, which is investor education and I'll close by saying this:

A lot of things we're going to hear today are, you know, really super important in terms of getting it right for companies, but as we try to balance this, you know, need for getting -- to having individuals get access to private market returns, many of these companies that are being financed are just riskier by nature cause their business models are earlier and a lot that -- comes a lot of volatility and a lot of risk, and I think it's our job to make sure that when people decide to invest in the companies that we're backing privately or publicly, that they understand the risks associated with doing that.

And so I'm very much in favor of what Commissioner Peirce talked a lot about. Investor education is really critical. There are many, many ways for investors to get access for -- uninitiated investors to get access to risky assets and we should be in a position where we are ensuring that when they make their investments, that they are fully aware of all the risks and that's going to be a big part of what we ultimately end up doing here for -- over the next -- you know, over the next day for sure, but in general, we make recommendations as a group.

So, I'm looking forward to it.

MS. GARRETT: Thank you, Jeff, for your thoughts.

I do not believe Hank has joined yet; is that correct?

(Whereupon, there was no response.)

MS. GARRETT: Okay. We're expecting him, hopefully, later after lunch, and we'll get his thoughts at that point in time.

So, Sue.

MS. WASHER: Hello. Thank you for having me today and I look -- I very much look forward to the discussion today cause some of the things that I've noted in my space of the public markets, which is a very specialized place of life sciences and biotechnology, kind of echo some of the things that both Jeff and Jason have pointed out, and that is that the IPO market, and biotech, and the life sciences remains very strong and the IPO window in biotech has been opened for a number of years.

But what we are noticing is that there is more and more in the crossover investors into the privates of companies -- very, very early private companies -- and by -- because those crossover investors are in, it seems to us that they're flipping to an IPO at a much earlier stage in the life cycle of a biotech than would be normal.

So, companies that haven't even entered clinical trial development for their products are going public at very, just astronomical valuations -- just numbers that you would never have seen even for a clinical stage company a few years ago.

And what is concerning about that is that once those companies are public, then you have your standard investors, generalist investors, retail investors trying to make decisions about companies that are in such an early stage of science, but I do think it's challenging for them. And so, again, investor education, I think, is really critical.

And then they -- what is coupled with this right now is that over the last few months, the follow-on markets for biotech companies has really cooled. So, if most of your IPOs are very, very early stage companies where it's going to be in biotech hundreds and hundreds of millions of dollars before revenues happen, but then coupled with that, you're having a cooling of the follow-on market, this is something I'm quite concerned about and I know others in our space are quite concerned about because how are those companies going to continue on the public markets without access to follow-on financing.

And so I'll be very interested today to learn more about what people are thinking about this huge increase in the crossovers and how that is changing. I was very interested to hear Jason say that this has really made those traditional venture capitalists get kind of priced out of working with these young companies and I really do think that the VCs are more experienced in working with young companies in biotechs and public market crossover rounds.

And so I really do think we need to be careful about this dynamic that we're creating so that the companies that do go public have ongoing access to capital and then we get these lifesaving advantages from new products on the other end. So, those are some of the things that we're thinking about.

Also, just a brief mention to SPACs, I think many companies in my space are trying to learn and really understand what the true cost of using a SPAC versus a regular offering is, and I think it's something that we're trying to -- companies are trying to educate themselves on.

And then lastly I'll just mention ongoing issues from the pandemic. You know, in biotech, a lot of what we do is science. You can't do science remotely; you have to have people in the office, in the laboratories doing the experiments. You have to have patients visiting clinical trial centers, and getting product, and getting tested, and so I think it's a unique challenge the pandemic has presented to biotech companies.

You've seen a lot of them have to change their guidance to the streets because they just can't get things done fast enough without full workforce involvement at -- in the office, at the clinical site. So, it's something that is still of a concern to us.

Also, with all of these companies going public at very, very early stages, the employment pressure is real. We're seeing it; very, very, very competitive employment marketplace when it comes to scientists, clinicians, MDs, quality control specialists, and this all does drive cost over time as well.

And so I think in the biotech space, we're still trying to work through that, figure out how to have people work at home that can work at home in order to have everyone safe that has to be at the office to do their work. So, that's just some of the thoughts that we have in the biotech and life science space.

MS. GARRETT: Thank you very much, Sue.

Greg Yadley.

MR. YADLEY: Good morning.

As a corporate lawyer in one of the largest states in the country, and the last Committee member to speak, I have -- I'm not going to repeat my experiences, which are pretty much the same as everyone else.

Florida has two-and-a-half million small businesses and three out of every four new jobs created in Florida come from those small businesses. That accounts for about 40 percent of the state's private sector workforce and about 44 percent of state GDP, and it's growing.

The pandemic has had major impacts on small businesses based on a couple of surveys I've seen. About a quarter of the businesses have reported lost revenue versus only six percent who reported increased revenue, but another 11 percent have closed.

Business owners have furloughed employees, implemented layoffs, and cut their own wages. So, there is a little bit of a rebound in hiring, but as Sue just said, you know, there's a lot of competition for jobs.

Again, from a couple of recent surveys that I've seen, 41 percent of Florida's small businesses have said that they have made changes due to COVID. Some are investing in handsfree point of sale systems, moving exclusively to digital marking versus any other kinds of marketing, adding new product lines, paint-at-home kits, anti-microbial products, anything -- you know, delivery -- and they're all struggling with what do you do about coming back to the office.

Law firms, being stodgy enterprises, have mostly just postponed mandatory go back to work, which in our firm was going to be in August and then September. It's now the end of the year, so probably 15 to 20 percent of our attorneys are going to the office every day.

There certainly has been some new business growth. In Florida, there were 98,816 new corporations formed last year. That's not much of an increase from 2019, but growth was, in limited liability companies, up 28 percent -- 383,575. Those numbers -- because Florida's economy is based in a lot of respects around agriculture and real estate -- a lot of those are just SPEs that don't really reflect actual new businesses. The corporate numbers, probably, more reflective.

One of the other things to keep in mind when you simply look at new corporate and other entity formations is how many of them survive. Barter ranks in the middle of the pack in terms of five-year start-up survival. So, only about 80 percent of the businesses created this year will survive for even one year. About half will be make it to 2025 and projected only a third will still exist 10 years after formation.

That said, in the Tampa Bay area where I live, there has been very good funding for start-ups. The numbers aren't huge compared to California or New York, but good numbers. In August 47-and-a-half million dollars was invested in start-ups, and that was almost identical with July, so the last two months total was nearly 100 million dollars, which is almost half of what was raised in all of 2020. So, it should be a good year.

I'd like to pick up on something that I think Bert said earlier about how the huge deal volume and interest in doing deals has impacted the legal and financial service asides. In fact, I got a call from an editor of one of our local publications asking for my verification. He has heard that some clients haven't been able to get their desired attention from professionals in order to be able to sell before the end of the year -- and higher taxes -- and I think that is an issue.

Certainly everyone that I know is fully engaged, but the lawyers at Shoemaker and our peered firms are of course committed to helping our clients get done what they want to get done.

So, we're not turning away business, but there is stress, and the other realty is -- especially in this pandemic period where it's hard, you know, to know what day it is -- but I think many of us are still feeling some nostalgia for summer. Kids going back to school and Labor Day really wasn't that long ago, but in fact, Friday is October. In other words, year-end is less than three months away.

So, given the fact that a lot of the deals being done are private equity driven and they're levered, due diligence just can't be done in a month for most deals. So, it is getting late and I think there will be stress to -- and people who want to do a transaction with any size -- certainly M&A deals -- but I think also capital raising need to get with their advisor soon if they want to get things done this year.

Thanks, Carla, and thanks to the Chair and the Commissioners for joining us this morning.

MS. GARRETT: Thanks, Greg, for those insights, and thank you to all the Committee members for your insights.

And next I'm going to pass it over to Jeff who will introduce our next topic.

MR. SOLOMON: Actually, if only I could figure out how to un-mute.

It's nice to -- thank you, everybody, for your feedback. It has really been a busy time, I think, for everybody, and I think this is obviously an important time for us to be thinking about how we move forward.

But getting each of your perspectives here is just such a -- such a really critical part of everything that we're doing and it really does -- I don't know about you all, but for me, it makes me feel like we're making a difference, and so being able to share our views, particularly to this group, is really informative. So, thank you, everybody, for doing that.

So, on August 1st, the Wall Street Journal published an article under the headline "Tech Start of Financing Hits Records as Giant Funds Dwarf Venture Capitalists", and the article was based on research conducted by analysts at PitchBook highlighting the increased investment activity by crossover investors, such as mutual funds and other investors that traditionally focus on public companies in late stage pre-IPO rounds.

The record level of financing for late stage companies is interesting for this Committee from many angles. Is it just late stage rounds or early stage companies also seeing change, and we heard a little bit about that. How's the presence of more passive larger investors impact more traditional early stage venture firms, something we've heard a little about that also. What is happening to valuation, which is a big part of the challenge when you're bringing in new capital, and how does this late stage financing help a company prepare for an IPO.

We are pleased today to have with us Dylan Cox, the head of PitchBooks' private markets research team that authored this fascinating report, and, Dylan, we look forward to hearing more about your analysts' findings and what you see happening -- changes you see happening in the pre-IPO capital raising.

So, I turn it over to you.

MR. COX: Thank you, Jeff, and thank you, everyone, for having me hear. Good morning, good afternoon depending on where you are in the world.

As Jeff mentioned, my name is Dylan Cox; I'm the head of private markets research at PitchBook. I have the pleasure of presenting to you today some of our research, as you mentioned, on crossover investing into venture.

My hope is to really paint a picture, provide more context, give some data to support the conversations that you all are having today, and frankly I think a lot of the data that we'll go through will be consistent with what many of you have already expressed about what you're seeing in your practices.

I'd like love to share my screen, if that's okay. I've got a couple of slides prepared for you. One moment here.

(Whereupon, a document was shared.)

MR. COX: All right. Can everyone see that -- that slide there?

PARTICIPANT: Yeah, I can.

MR. COX: Great. Thank you.

Before we get started, I'd like to note that, you know, this is not -- I did not write this piece of research, but our team at -- the institutional research group at PitchBook did.

My colleagues, Cameron Stanfield, Joshua Chou, and Kyle Stanford specifically worked on this research and lead our venture capital efforts more broadly.

Quick, obligatory commercial or informercial for PitchBook, for those of you that are not familiar with our work. We are a research and data provider, not just for private markets, not just for venture capital, but for public markets as well.

We cover the entire private capital ecosystem from the VC deals that are getting done to the VC funds participating in those rounds, and any institutional investors investing in those venture funds as well. We cover not just venture, but private equity, private debt, secondaries, real estate -- really, the entire private capital ecosystem.

All right. Back to the research:

There are a few key questions or considerations I'd to frame our conversation around today. The first is how prevalent are crossover investors in the venture capital ecosystem. Given I'm here speaking to you all about it, I'm sure you can guess that they're quite prevalent.

The second, what are the motivations for these crossover investors and in turn, what are the motivations for the companies raising capital from these crossover investors. The third, how has their involvement affected VC-backed exits and specifically, we'll look at IPOs. And, lastly, do these investors have staying power within venture; are they what we refer to as "tourist investors" in venture or will they be here for years or decades to come.

Before we really begin, quick definition of terms so that we're all on the same page, who are these crossover investors; what do we mean when we use this term.

Crossover investors are a subset of what we generally refer to as nontraditional investors in the venture ecosystem. So, these nontraditional investors are typically mutual funds, hedge funds, corporate venture arms, and other large asset managers who also invest in venture deals. Crossover investors are typically bi-side public equity managers that also invest in privately-backed companies.

A few examples of crossover investors, some of the most prominent ones you can see here. Well-known firms like Tiger Global, OrbiMed who invested in life sciences and biotech space, Coatue Management, T. Rowe Price, Temasek, Wellington Management, Fidelity, and BlackRock to name a few. So, again, really well-known -- in some cases, you know, household names in the public equity asset management space.

It's worth noting that our specific methodology for this research defines crossover investors hedge as any hedge funds, mutual funds, sovereign wealth fund, or other asset manager that has participated in at least 10 VC deals since 2015 and doesn't primarily invest in the venture capital. So, all of the firms on this slide meet that criteria.

Back to our key considerations, how prevalent is crossover investing in the venture ecosystem. Short answer is, very prevalent. In 2020, VC deals with crossover investor participation totaled about 60 billion dollars -- just over 61 billion -- across more than 700 deals.

That's about 36 percent of the total dollar value of these deals, suggests over a third -- but only about five percent of the total number of transactions, which tells us that crossover investors -- or excuse me -- crossover deals tend to be much larger than your average VC deal.

It's not just that crossover rounds tend to be larger, but the average size of these crossover rounds has been growing over time and this reflects trends that I'm sure all of you have seen in your practices and trends that we see in the data for VC more broadly over the last decade or so, and these two phenomena, I believe, really feed off of one another.

Crossover participation pushes round size up -- round sizes up while the larger round sizes entice more traditional public equity asset managers into the VC space as they're able to deploy capital without writing so many checks.

Not surprisingly, crossover investors tend to invest in the later stage -- later stages of venture capital, which account for more than half of all crossover deals in each of the last few years, but it's worth noting and it has already been noted by a few of you today, that crossover investors are involved also in early stage venture capital, even in seed stage deals. They're not the majority of crossover deals, but these investors are prevalent at the earlier stages.

So, next key consideration for us, what are the motivations for these crossover investors. As I'm sure you're all aware, the number of publicly traded companies in the U.S. is well below what it was a couple of decades ago. Most recent data I have from the World Bank shows that in 1996 there were more than 8,000 listed companies in the U.S., and each year since the global financial crisis, that number has been fewer than 4,500. So, hardly more than half the number of publicly traded companies.

At the same time, the amount of capital chasing these companies has really ballooned, so, alpha is harder to come by from any other these investors, we believer. At the same time, start-ups have been staying private for longer often because there's simply plenty of capital available to them in the private markets. Over the last decade or so, there has -- there hasn't been a need to go public as soon as what had been the case maybe a decade prior to that.

For investors, they don't want to miss out on value creation by waiting for an IPO. By participating in these pre-IPO rounds, crossover investors are typically able to build ownership at a price below the eventual IPO price or at least that's their aim. Generally, they're searching for companies with a clear path to profitability and superior growth prospects relative to private markets.

They're looking for IPO candidates and usually like to hold the stock for a few years post-IPO. It's also worth noting that these crossover investors tend to be more hands-off and less price sensitive than traditional VCs. This -- their hands-off approach really allows for syndication or participation amongst or between crossover investors and traditional VCs in the same financing rounds.

For companies raising capital from crossover investors, we really break this down to two different buckets. The first is those with a clear path to profitability or maybe just later stage companies that are closer to IPO.

For these companies, the crossover round often provides a tangible evaluation prior to the IPO, sort of a high water mark to move from. It brings credibility and prestige to the capital table, increases capital availability. It is a capital raise after all and it streamlines the path to going public. Crossover investors tend to double down and also invest during the IPO round as well.

Now, for those companies without a clear path to profitability or maybe just earlier stage -- deals -- Series A, Series B even -- these rounds often serve as a large capital raise use for scaling research and development, could be building infrastructure, requiring critical massive users -- really focused on growth.

They're either focused on that growth or it may be that the nature of the industry requires lots of capital prior to producing profit or even prior to producing revenue. I'm thinking of companies in the biotech and pharma space, start-ups that are maybe in the electric vehicle space, air taxis recently, climate tech solutions -- things of that nature that will take years and years of development prior to producing revenue.

Next key conversation for us, how

has their involvement, meaning crossover investor involvement, affected VC-backed exits, and specifically, we'll look at public listings.

The public listing is where crossover investors should really prove their value to these companies; unlike traditional VCs, which tend to be more hands-on pre-IPO as opposed to during the IPO or after it. Since they mostly invest in public markets, crossover investors' presence should be a positive sign, which should help build a book of investors at the IPO.

Companies, on the other hand, may prefer crossover investors known for being long-term shareholders rather than those looking for a quick flip. We mentioned that these investors will often hold their stake for a couple of years post-IPO, and this can create some price stability for newly public businesses even after any lock-up periods.

It's worth mentioning again, by participating in these pre-IPO rounds, crossover investors are typically able to build ownership at a price below the eventual IPO price.

As we can see here on the slide, the dark blue bars at the bottom are rounds with crossover investor participation prior to an IPO for a VC-backed company. So, about 75 percent of deals in 2020 of the dollar value deals had some sort of crossover investor participation prior to IPO, and that number has crept even higher through mid-September in 2021.

We see the same trend when we look at the number of IPOs as opposed to the dollar value of these deals. Crossover investors are really becoming ubiquitous in these cap tables. In 2020, they were present in 77 percent of IPOs by values, as I mentioned, just over three-quarters.

Pardon me -- wrong slide here. And when we look at the number of deals here, they are present in 74 percent of deals, so it doesn't really matter whether you're looking at it by dollar value or the number of deals. Crossover investors are quite prevalent in the IPO space.

Since 2010, this trend has been on

the rise mirroring the growth, again, that was seen in private markets more broadly and venture capital specifically, and even more specifically by nontraditional investors in the VC ecosystem.

Another question we looked at in the research is what effect, if any, do these crossover investors have on the valuation step-up -- the increase in enterprise value at the time of IPO, and we find that actually IPOs with crossover investors tend to have slightly smaller increases in valuation or step-up at this time. This varies from year to year, but as a whole, it is a slightly smaller step-up.

This is somewhat expected though because of the larger size of the IPOs with crossover investors, and if you think about it, the, perhaps, difficulty in growing enterprise value on a percentage basis was such a large valuation to begin with.

Also, it's worth mentioning -- and someone alluded to it earlier -- that the time between the last crossover investment and eventual IPO has trended down recently. That's medium time to IPO -- excuse me -- between crossover investment and IPOs, just about six months, meaning there's less time for value creation between those two rounds.

Our last key consideration or question for the day is do these investors have staying power within venture. Do we expect them to stick around. Short answer is yes. We look at the data -- the percentage of crossover rounds where that crossover investor was the lead investor on the deal, meaning they are the ones negotiating terms and price on the deal.

The percentage of those deals have been rising in recent years now sitting at about half of all deals. This means that crossover investors are becoming more active participants in these rounds. They're not just providing capital, and checking, and -- you know, every quarter or every year.

As crossover and nontraditional investment continues to rise, their strategies have really evolved. Some of them are even raising specialized venture focused funds with investment teams that are, again, focused on these strategies and should really enhance their sophistication when it comes to negotiating these prices and terms. It's not a mutual fund manager investing in these venture deals in most cases.

Some analysts worried that the pandemic would push these investors back towards their core strategies, usually in public markets, but instead we've seen them really double down on venture. That same trend is seen again when we look at the number of deals rather than the value of those deals.

Crossover investors taking a lead investor roll has only continued to rise into 2021. In total, the motivations for these investors are clear. There's more value than ever before being created in private markets, pre-IPO, and investors want to participate in that upside. Investors in these funds -- in the crossover funds, themselves -- so, the other institutions and individuals -- investing in these funds now often expect some sort of exposure to private high growth companies.

Creating alpha or least perceived alpha from participating in these private investments is likely to keep capital flowing into these crossover investment funds.

So, in conclusion, we believe, you know, all of these factors will fuel venture activity more broadly and crossover participation in these deals, more specifically, for the foreseeable future.

That's all for my prepared remarks. Thank you again for allowing me to present our research today and I'd love to pause here and answer any questions you may have.

MS. GARRETT: Thank you very much, Dylan, for that presentation.

Do people of the Committee have questions for Dylan? If so, if you want to put your name in the chat, then I can call on you.

Hi, Jason.

MR. SEATS: Hi. Hey, Dylan. It's interesting research. Thanks for it and for everything you guys are doing at PitchBook.

So, I guess I have a question about maybe just motivation. You know, part of my story line narrative perception is that these crossover investors, who are also investing pre-IPO, actually -- not only are they deploying, you know, larger dollars and whatever else -- they can make them less price sensitive -- but that they're, in many respects, not focused on the return profile of the private market investing at all and are merely kind of securing their place, sort of skipping the line on the go public process, and that it has obvious sort of negative feedback loops on pricing in private markets.

I was wondering if you could comment on that or if you have any sort of narrative on the motivations there.

MR. COX: Sure. I view it as a bit of both focused on returns or value creation within private markets, but then also to your point, building ownership in the company prior to IPOs or skipping the line, if you will.

We do see, in most cases, between crossover investor involvement and an eventual exit, we do see growth in enterprise value in valuation over that time. So, I'm sure there are -- these investors are focused on returns, though they are less price sensitive. They are not beholden simply to the private market returns, like traditional VCs made.

This has, of course, pushed up valuations in venture more broadly. It's not the only thing that has pushed up valuations. You know, you could point to any number of things to recycling of capital into these funds. A lot of folks are pointing quantitative easing; just, you know, increasing the amount of capital capability more broadly.

And, of course, it's not just venture capital where we have seen increases in valuation pricing; it's happening in public markets as well.

MR. SEATS: Do you all happen to have any data on sort of the magnitude of dollars deployed by these firms pre-IPO and post?

In other words, is it -- are they putting ten times as much money to work pre-IPO; is it, you know, post-IPO? Is it 50/50?

MR. COX: We have a harder time tracking their capital deployment post-IPO.

So, pre-IPO, I think in 2020, the data was about 60 billion dollars in the U.S. and 700 deals or so, but we don't know quite how that relates to their post-IPO capital deployment.

MS. GARRETT: Jeff, did you have some

questions?

MR. SOLOMON: Yes, I'm curious to know, if you dig in on some of the numbers that drive this -- cause these are great outlets -- it's a great presentation and, you know, as a subscriber to PitchBook, I think what you guys are doing is great cause it's super helpful for us to understand these trends and we are subscribers, so full disclosure.

MR. COX: Thank you.

MR. SOLOMON: You know, one of the things that we're seeing -- and I was wondering if you can, you know, validate this or invalidate this -- or maybe you just don't have a view -- but there are few things, I think, at play here.

One, public company investors are much bigger than they used to be. So, when you think about sort of -- I always go back to the year 2000, last time we had a lot of IPOs and a lot of public companies -- the end of the 90s. You know, you didn't have multi-trillion dollar asset managers back then and now we do.

And so when you look at their ability to generate returns, they almost have to go earlier in the life cycle of a company in order to ensure that they're getting -- in order to ensure that they're actually getting a meaningful investment in these companies.

So, the crossover development over the last decade, I'm just asking, do you think it's as much a part of the fact that they need to get these anchor investments so they can put a significant amount of capital to work in the IPO and beyond or is it -- or are they just chasing returns, you know, in venture-type oriented stuff because they have to be able to generate, you know, alpha in their own?

I mean, I'm -- or is it both?

MR. COX: My view would be it's a bit of both. You know, we mentioned in the presentation, alpha is harder to come by depending on how you measure it. You know, price of earnings, multiples for the S&P 500 are as high as they've been in the last couple of decades.

So, it is generally harder, maybe, for those private public market investors, but there is an element of return chasing here. Private capital returns have been quite string for the last couple of decades and I think public market investors have sort of developed a bit of jealousy there, right.

You know, how do I invest in these -- in the next Facebook, the next Uber, the next Airbnb sort of thing -- and we are seeing larger capital raises, not just from crossover nontraditional investors moving into venture, but from venture funds themselves. That's all they do.

So, we think about the -- Sequoia Capital has raised a few funds that are in the billions of dollars. The SoftBank Vision Fund raised 100 billion dollars a few years back just targeting late stage venture. That's frankly incredible that anyone would target this space with that amount of capital, and that has had a big impact on valuations and returns in the space too.

MR. SOLOMON: And then one other question before -- I see that Sue wants to ask a question too, which I'm sure will be biotech focused, so I'll ask this --

How -- I mean, I'd be curious to see the aftermarket performance when you have VC investors and crossover investors at the same time.

You know, the dynamic, I think, that we're seeing that has really been an unlocked for capital formation has been that there was a lot of tension between venture capitalists and public company investors for public market investors for a lot of years because there was a view in the public markets that venture investors were moving up valuations in order to get public market investors to pay up, and, of course, public market investors want to pay cheaper and venture investors always want to -- there's always that price tension.

One of the things that crossovers have done is you're actually both groups to invest in a new round, which allows for the venture capitalist to say, "We still think there's value to be created from this point and we want to partner with the public people -- with the public company investors who are going to be our anchor investors going forward".

And what's that has allowed for is managements teams to actually bridge the gap between your old investors and your new investors, and maybe it makes it a little easier to deal with lock-ups and selling post -- and I'm curious to know if that has been something that you've explored and if you've looked at the performance of companies that have gone public that have both VC and crossover investors, and is that a trend you think will continue.

MR. COX: It's not something we've explored. Frankly, it's something we'd love to or would work well in our research pipeline, but we haven't had the bandwidth to yet.

Your comments do remind me though of the sort of public discussion that has been happening around direct listings in the last couple of years, right. VCs have been huge proponents of using direct listings as opposed to a traditional IPO round, you know, thinking that those public asset managers and the investment banks are taking a lot of the upside in the IPO away from the VCs.

So, I don't have strong data there, but that's sort of where my mind goes.

MR. SOLOMON: Okay. Thank you.

MS. GARRETT: Sue, did you have some

questions?

(Whereupon, there was no response.)

MR. COX: I think you're muted, Sue.

MS. WASHER: I was. Thank you for the opportunity to ask a question and, Dylan, thank you for your presentation today.

I guess, I have another question along the lines of what Jeff was speaking on and that is, you have a lot of data on what this means for those crossovers investors and, you know, their ability to be kind of chasing alpha and maybe skipping the line and participating in gaining value.

My question is around the fact of, what is this doing for the companies, themselves? How are the companies performing overall and is it -- is there any data showing that getting these crossover investors earlier is helping the health and success of the company? Is it having no effect; is it having a detrimental effect?

And then kind of part of that question is, you know, it seems to be that's a very quick term between the crossover investment and then the IPO, like five or six months. That's barely enough time. Most companies take longer than that to get ready and do an IPO and so, you know, how much value is really being created during that five to six months to justify an increase or a step-up in price at the IPO?

And then, as I said, what happens to these companies afterwards, especially the ones that are getting out so much earlier than would normally be the case?

MR. COX: Sure. So, I'll take that in a couple of different parts.

The first is, you know, what's the difference in outcome or what value add are the companies getting? we don't quite have the data to be able to explore that. It's hard for us to look at outcomes on a company by company basis. Generally, with returns and private markets, we look at fund level returns. That's just sort of how we're able to come across the date and slice it more easily.

But one, I think, clear benefit, more anecdotally for these companies, is that the capital raises tend to be larger these rounds. These -- you know, talking Tiger

Global, or Fidelity, or some of these other big names, they do tend to be less price sensitive is what we're hearing from firms.

And so you're able to -- you know, you're raising more capital and maybe you're giving up a bit more ownership in your company, but your able to do it rather quickly and know that you likely won't run out of capital in the near future, sort of extending your runway a bit further than you would've otherwise.

But I agree with you that the time between pre-IPO round versus the last crossover round and the eventual IPO, at just about, you know, an average of about six months I think is what our data says -- that's quite quick and not a lot changes a lot of times in six months.

And this, I think, is -- these rounds, often over 100 million dollar capital raise, we often just refer to it as pre-IPO rounds whether or not they proceed in IPO because that's usually the assumed intention, if you will, is just sort of, you know, pulling some of that -- that IPO capital raised forward because you can. It's not something you used to be able to do in private markets, is have that investor base available to you.

MS. WASHER: And just a quick follow-up, Dylan.

Do you guys have any information about what I spoke about earlier, in that it's starting to be felt in the marketplace at the -- while the IPOs are healthy, and happy, and a good clip, and raising a lot of money, that follow-on financings for existing companies, at least in the biotech space, seem to be very, very soft right now?

MR. COX: I don't have the data in front of me. We do have an analyst on our team who covers biotech, so I'd love to check in with him and his research and report back, but I don't -- I'm not familiar with the data myself.

MS. WASHER: Okay. Thank you.

MS. GARRETT: Hi, Martha.

MS. MILLER: Yes, Dylan, thank you very much for coming and presenting this information.

When I first saw the report come out from PitchBook, I was thinking, somebody else has got to be writing about this and covering it, and sure enough, a couple of days later Wall Street Journal picked it up and it started making the rounds because it really is interesting research highlighting dynamics that I don't think a lot of people have really paid attention to. They see the aggregate numbers of what is happening in late stage capital raising, but not where that money is coming from.

My question for you, looking at distribution -- and this may be something that you haven't looked at -- but our office is particularly interested, not just in the data and macro trends, but really slicing that and looking at what is the impact on under-represented founders and their investors and women -- people of color -- those in different rural communities or areas impacted by natural disaster?

I'm curious from the data -- I think Jason said it was the usual suspects -- or I think Jason had a great phrase earlier when he was giving his update about -- typically a lot of what they're seeing is chasing after our, you know, prototype of kind of a successful white male in Silicon Valley.

Is there where a lot of this capital is headed; what is the diversity portfolio of these investments? Are there any interesting trends that you're seeing there along demographic lines that we should be paying attention to?

MR. COX: Sure. So, it wasn't a part of this research in particular, but the sort of under-representation amongst female founders and more diverse founders -- founders of color -- has been well reported both by PitchBook and by other firms. It certainly an issue in the industry.

One thing I can shed light on is we have a piece of research that came out just a couple of days ago looking at where graphically venture capital is being allocated in the country, and more than half of all VC deals in the U.S. still have been in the top four ecosystems. So, that's the Bay area, Los Angeles, New York, and Boston account for more than half of all VC deals and dollars.

And so it -- yeah, it often is sort of serial entrepreneurs or, you know, folks who have been in that ecosystem for a long time. There have been some, you know, well publicized attempts to start to change that -- the Rise of the Rest Fund is one that comes to mind. BackStage Capital is another who specifically targets more diverse founders, which full disclosure, I'm an investor in.

But we haven't yet started to see, I think, material changes when it comes to capital flowing to more diverse founders. The numbers are still, frankly, very, very lopsided.

MS. MILLER: That's very helpful because one of the things, especially as you look at the really earlier stage activity with crossovers, is wondering what is that nexus in connection for identifying those opportunities, and from what networks are those deals being forced, and what do we need to be thinking about from a policy perspective to ensure access to opportunity for those who may not be within the personal networks -- the professional networks -- of those who are out seeking this deal flow.

MR. COX: Absolutely.

MS. GARRETT: Anybody else on the Committee that's interested in asking a question?

MS. MEHTA: Just to get a little more granular, you said that still more than half the deals are done in those large four markets.

Has -- I know it used to be between 75 and 80 percent -- maybe it was previously -- had -- to be -- get a little more granular, is it still hovering around that percentage or has it -- do you think it's a little bit more disbursed now?

MR. COX: I may have the data right here in front of me -- (perusing) -- I don't. I'd be happy to report back on that. This is research from just a couple of days ago that our team put out.

New York, Boston, Los Angeles and Bay area-based VCs have raised more than 1,400 venture funds since 2018 and amassed 216 billion for investment -- where is this -- (perusing) -- here we are.

So, speaking of valuation, these ecosystems, late stage valuations in those top four ecosystems has more than tripled in the last decade. But if you look at the six VC ecosystems past that, valuations in the last decade have grown by just 49 percent compared to 300 percent.

So, I don't know if we're seeing a trickling down to those sort of lesser known ecosystems. A lot of those headline numbers are still very much driven by San Francisco, New York, Boston, and LA.

MR. SOLOMON: No, what we're seeing is certainly a willingness of public market investors and crossover investors to be less geographically focused. You know, they generally look across the broader landscape in the United States. Their biggest, I think, concern or their biggest gaining item is how long will it take to get the company public?

So, even when you look at crossover investors and the amount, I would say it -- generally speaking, our experience is that crossover investors are looking for companies to get public at some time between 12 and 24 months after doing a crossover round, and when the market -- public markets back up, you can see it slows down significantly, right.

They all have only a certain percentage of their portfolios they can allocate to private securities, and if the public markets or the IPO markets slows down meaningful, a crossover market also slows down meaningfully until those shares are registered. It doesn't mean they're selling; it's just they need them to be not private and they need to make sure those shares are registered in order to, you know, relieve them of the sort of the illiquidity profile in their own funds.

But they're willing to go just about anywhere if they think a company is meaningful enough, and they're willing to collapse the timetable between -- in fact, they prefer to have a collapsed timetable between a last -- you know, a venture round, a Series A, a Series B, or a Series C, a crossover, and an IPO -- their view is it's an accelerant to getting a company public.

That's like, I would say, probably a bigger gaining item on crossover investors, and I see, you know -- you know, I see you shaking your head no and so I'm guessing there's some feedback that's consistent?

MR. COX: It makes sense to me. We don't have the data to support it. Certainly with more sort of zoom focused capital raises would make sense to me.

Any other questions?

MR. SOLOMON: Yeah, is there any -- I just want -- is there improvements to the crossover market that you've heard about or that you're aware of that you think we should consider to continue fostering that or protections maybe in the crossover market that you've been aware of in your studies, other than just presenting the data, that we consider maybe as a result of this data?

MR. COX: Meaning investor protections around transparency and that --

MR. SOLOMON: You know, things that you've heard in your work around -- that investors are concerned about that can be addressed or things that we should be concerned about that maybe we haven't considered, given the explosion in activity in the space.

MR. COX: The main thing we hear about is, frankly, from traditional VCs, that they -- that crossover investors are driving up valuations to sort of an unsustainable point in the space. That remains to be seen whether or not that's true.

You know, we'll see if these companies, even at sky high valuations, are able to exit to public markets at an even higher one. I think valuations in private markets tend to take their cues from public ones, so as long as we see higher price multiples in U.S. public markets, we'll see a similar phenomenon in private ones.

MR. FOX: Jeff, on that point -- and I'd be curious if Dylan has the research to back this up or not -- but my personal experience over the last year has been is that a lot of these crossover investors, because they are actually -- to your point, they're not all selling out at IPO, it is allowing for a number of situations where the actual offer -- like the cash needing to be raised, especially in more capital intensive industries -- is actually lower, which actually enables, probably, a more successful IPO, right, cause they're not having to raise as much on pricing because you have investors that are actually hanging around for a little bit of time.

And so from that perspective, you know, there does seem to be some attractiveness of getting that cash in and then going public with a lower capital raise, right, through the IPO process. But, Dylan, I'm curious if you're seeing that trend, if that's beyond just what I've been seeing than the deals we're looking at in our firm, so --

MR. COX: We haven't seen that in the data; we haven't looked at it as part of this research. So, that could be one potential explanation for having a pre-IPO round just five or six months prior to IPO as it closes to your point; getting some of that capital on board before the sort of formal IPO.

MR. SOLOMON: And, Bert, here's something that I would just offer that -- and then I know we're going to run up on time here.

So, when we're launching a lot of IPOs -- again, biotech or non-biotech -- you know, I think what we're seeing is that we want those IPOs to be pretty well covered before we launch, meaning that we have a pretty good idea that if we launch an IPO, that it's likely to be able to raise the amount of money that we stated.

And a lot of that capital, or the anchor orders, come from those crossover investors because they're going to be taking meaningful amounts of stakes. They've also been trained to know that if they don't participate in the crossover -- if they don't participate in the IPO commensurate with the size of their crossover, they're going to be excluded from the next crossover.

MR. FOX: Mm-hmm.

MR. SOLOMON: And so there's definitely a tension that is an intentional tension to make sure the crossover investors are going to be there for the long haul and become solid long-term shareholders of companies and that --

MR. FOX: Mm-hmm.

MR. SOLOMON: So, what we're seeing is most of the IPOs that are launched -- the ones that are successful -- they generally are going out there with significant anchor investors already. And to the likelihood that you don't get a completed IPO has actually gone down considerably and it would be an interesting statistic to look at of IPOs launched and failed prior to the crossover.

And I think -- I mean, I don't -- I'm guessing just based again anecdotally on some of the data -- and I think it would be great if PitchBook had this data or if they have access to it pretty quickly -- if you could see, not just the -- if you could see the actual difference in the persistence of the IPOs launched and completed, where there were crossover investors versus IPOs launched and not completed and whether or not there was a correlation to whether or not they had crossover investors.

And I think what you'll find is that there's just a lower probability -- significantly lower probability that you don't get an IPO done --

MR. FOX: Mm-hmm.

MR. SOLOMON: -- if you have a crossover round. That's just -- I think, anecdotally, we see that. It's certainly advice that we give to companies all the time before we advise them to go public -- certainly smaller companies.

MR. BERT: Yeah.

MR. SOLOMON: And I would say that's -- you know, we're advising them to do a crossover round before accessing the public market.

MR. FOX: And, Jeff, just to clarify, part of my point, which I think echoes what you just said, is because bankers in a lot of cases do want the deals to be over-subscribed to certain multiples, right, going -- if you need 200 million and you've gotten, you know, 100 million or 75 million of capital in a pre-round, going for less allows you to get that over-subscription as well, right, was part of the point I was making as well, which, again, gets back to a higher likelihood of a successful offering, so --

MR. SOLOMON: There's also a feedback loop here that I think is important because for those of -- those of us that worked on the -- you know, on the Jobs Act, the test the waters component, which really opened up the opportunity for private companies to engage with investors more broadly before actually filing a registration statement.

There was always a concern around gun jumping and Section 5 violations and that sort of obviated -- that legislation gave companies the opportunity to go engage crossover -- what are now crossover investors or public company investors.

I think that the thing that's happened there is oftentimes we're getting feedback that the company is too early for an IPO, and that doing a crossover enables the company to stay private longer to meet more of its -- you know, more, you know, benchmarks or milestones prior to accessing the public market.

And, you know, there's no question that people are completing their crossover rounds and then immediately starting their IPO process, but what we're trying to do is see that there is some real value inflections and that the crossover round itself -- in and of itself -- actually enables the company to stay private longer to round out its management team, to do other things that we think are really critical for it to have better experiences in the public market.

And prior to the Job Acts and prior to the explosion in public funds doing crossovers, that just wasn't available, so I think this is just -- it's important to note that this is part of the vital ecosystem of helping smaller companies get from the 250 million dollar market cap. Oftentimes, that crossover round is the thing that enable them to get a different place, you know, and maybe even get public at some point.

And I think just to tie it back to why we're talking about this, that's just an important part of the ecosystem. It's just a little bit -- you know, folks own companies a little bigger than the ones we traditionally focus on -- but that path has enabled many, many, many companies that are sub 250 million, particularly life sciences, to get access to capital, you know -- and, you know, wonder whether they're actually going to be able to work as public companies.

MS. GARRETT: Hi, Hank. Welcome to the meeting. We see that you have a question.

MR. TORBERT: Yes, I do.

Dylan, firsts of all, thank you for your great research and all the work you've done.

I have a simple question, which is when you think about industrial corporate VCs and so on, is there a correlation with them and crossover investors because if you have a strategic investor or someone who vouches for the company by putting money there, is there a high correlation between those and crossover investors?

MR. COX: We're not able to look at the data returns for individual deal like that. I will say though that the -- in the methodology for this research, we excluded corporate venture arms. We do, however, include them in sort of the nontraditional bucket in a lot of our research.

So, most of this crossover investing that we discussed today is more traditional, kind of VC sectors, like software is the largest one --

MR. TORBERT: Right.

MR. COX: -- and then biotech and pharma is a large chunk of it as well.

MR. TORBERT: Right. Okay. Thank you.

MR. COX: Sure. Thank you.

MS. GARRETT: Okay. With that, Dylan, thank you very much for your presentation, for all your information, for all the statistics. I think we've all learned a lot as a Committee.

And, Hank, before you got on, and since we have a few minutes before lunch, if you would like, we each -- each of the Committee members just went one by one and talked a little bit about what we're seeing right now in the market -- You know, the effects of COVID.

If there's anything you'd like to discuss or mention, we wanted to make sure you had an opportunity to speak also.

MR. TORBERT: Thanks -- thanks for that.

Of course; I mean, we've just gone through Hurricane Ida here in the Gulf Coast, so what I'm -- I'm seeing a couple of things.

One, the -- how many of the small businesses are in fact having trouble getting financing to support their operations and how thinly supported they have been.

So, again, it shows how important it for us to focus on making sure that owners of any type, especially small business owners, are getting access to capital they need cause I've seen a lot of businesses go under right now as result, notably in the smaller industrial sector and so on, which is where I focus.

That's it.

MS. GARRETT: Okay. Thank you.

Okay. With that, we will take a break for lunch. The webcast will be stopped and we will resume at 1 o'clock. So, we look forward to having all the Committee members back at 1 o'clock.

And once again, Dylan, thank you very much for your time and for your presentation, and it was a pleasure having you with us today.

MR. COX: Yeah, thank you so much, everyone. It was a pleasure to be here.

MS. MILLER: Agreed. Thank you, Dylan.

(Whereupon, a brief recess was taken.)

MS. GARRETT: Welcome back, everybody,

from lunch. We are thrilled to start with our new topic -- or next topic, which is a nice segue from our early-morning topic, which is the changing dynamics of IPOs, direct listings, and SPACs.

There are multiple paths for companies to join the public markets, from traditional IPOs to newer direct listings, to the reemergence of mergers with special purpose acquisition companies -- SPACs -- and so we've invited a panel of experts today to share their experiences with how companies and investors are weighing the different pathways to become public.

Our goal today is to begin to form some sort of broad themes or frameworks to help guide us when we consider, as a Committee, recommendations in response to rule-making initiatives that the Commission may have on these topics, which we understand may be in the Commission's near term agenda.

We will first -- I'm going to introduce one speaker at a time and let the speaker present, and just so everyone knows the order of the speakers, it will be David, and then Phyllis, and then Michael, and then Isabelle.

So, we'll first hear from lawyer, David Ni. He is a partner in Sidley & Austin, LLP's New York office and he's a co-leader of the firm's SPAC group. David represents issuers, underwriters, and selling security holders in a variety of public and private offerings.

David, we look forward to hearing your perspective on the differences between the various pathways and how they work for smaller companies.

MR. NI: Great. Thank you, Carla, and thank you to the Committee for having me. I'm very happy to speak on this topic that, you know, I pretty much spend my career doing since 2008.

My goal is really just to give the Committee an overview of the different paths to being a public company, and I would actually start off by saying that there's roughly two general paths to the going public, of which under each is two sub-paths. But, generally speaking, you know, you can go public -- as a private company, you can go public through one of two general ways.

One is you can register an offering with the SEC and the U.S. Securities; so that's what it means to go public. It's being registered -- having done a registered offering with the SEC, and having listed securities.

And the second way is just merging with or being acquired by a public company, because, of course, if you merge with or get acquired by a public company, you can indirectly become a public company.

And then underneath each of those, you know, in terms of just registering with the SEC and listing, the classic example -- the one that we're all very familiar with -- it's just an initial public offering, where a company goes ahead and does an offering, issuing new securities, in some cases, registering the offering of securities held by its existing shareholders and -- with the SEC, and then listing the securities on Nasdaq, New York Stock Exchange, or one of the other exchanges.

A newer variant of that is that -- are direct listings, which, you know, we've all been hearing a lot about. With a direct listing, it's not that much fundamentally different from an IPO in terms of the registration process. You're still registering with the SEC and you're still listing securities on the stock exchange, but there are obviously a lot of key structural differences in terms of how the offering takes place.

In the other category of just verse merging or merging with a public company, one method has been around for a very long time. I mean, that's just, if you get acquired by a public company, right, either you merge with and they survive or you become a sub of a public company. Those are generally with, you know, operating companies.

If you're a sugar manufacturer and you get acquired by Coca-Cola, you now have indirectly become a public company, albeit, as a subsidiary of Coca-Cola. So, that has been around forever, but that's usually not seen as a pathway to going public because no one really plans those.

You know, you don't start off as a private company thinking that my way to going public is to try to find a big operational company to buy me out. Those happen very opportunistically. And then the second subset of just merging with or being acquired by a public company is, of course, SPACs.

SPACs have been around -- you know, a lot of people think SPACs are a very new phenomena, but that's not true at all. I mean, the earliest SPAC, that you can trace it back to 1881. That's the earliest known semblance of a SPAC.

The current generations of SPAC really derive from the blank check companies of the 1980s, which, unfortunately, were largely associated with penny stocks and pump-and-dump schemes. You know, you have these, think "Wolf of Wall Street" type of people who would create these blanks checks.

They'd be thinly traded, so there'd be a lot of volatility. They'd put on a bunch of false information to get the stock prices up and then flip them.

So, that was the earliest iteration of the current generation of SPACs, and then around 1993, a banker and a lawyer worked with regulators to come up with a lot of protections to help, you know, make the structure more mainstream and less, you know, prone to abuse. So, a lot of the features that we know today, like redemptions and putting money in trust, those are very much, you know, designed around the early 1990 -- 1993 roughly.

And since then, you know, there have been handfuls of SPACs and there have been periods where it has been very poplar and periods were it has not been, but even at its height, it has never been as popular as it has been now, and it's history is, you know, very much up and down, and responded to all the major events in our capital markets.

Like, for example, during the tech era, SPACs basically disappeared because IPOs in 2001 were just so easy to get done, so no one was even looking at SPACs. But then when the IPOs fizzled -- tech IPOs fizzled, in between that and 2008, there were periods were there was a small resurgence of SPACs, and then around 2008, they died again.

The most current wave of SPACs really began in 2019 when -- if I had to trace it, I would say when Virgin Galactic went public through a SPAC and that really got everybody's attention in 2019, and it performed extremely well too.

So, suddenly you have a lot people looking at the structure and seeing the stock price go from $10 to 40, 50, 60, right, and that attracted a lot of attention, and that was immediately followed by a bunch of other blockbuster De-SPACs -- you know, Draft Kings, Nicola, etcetera -- and so that brought a lot of attention to SPACs.

You had a lot of other events that really contributed to the rise of SPACs, at least in its current generation, but, you know, you had historic low interest rates, which, of course, vary much, and then people wanted to deploy capital and not just let it sit around in bank accounts, and why not a SPAC where you have this downside protection, but then you also have this one in a million chance of getting this extreme upside.

You have media attention, right, which also contributed to the popularity of SPACs; retail interest -- the rise of the retail investors. You know, the $10 per unit in SPACs, I mean, that was built -- that was custom designed for retail investors because everybody can afford $10. I mean, not everybody can put up the million dollars to invest a true private equity firm, but $10 a unit, you know, my grandma can do that.

You know, and then there's a bunch of other factors too. I mean, you have celebrities piling onto SPACs, right. Everybody who is anybody had a SPAC or was associated with SPAC. So, due to all of those factors, I mean, you've seen just a huge, huge surge of popularity in SPACs and I'll show you some, you know, basic statistics to really highlight the point.

You know, in 2017, there were 34 SPAC IPOs and that was considered a great year for SPACs. It has never been that high. 2018, 46; it was almost 50 percent higher, and that was considered banner year. 2019, 59; you know, it just kept going up. 2020, 248 SPAC IPOs. Year to date, 2021, 441 SPAC IPOs. So, it's more than a hockey shape; it's a -- hockey-shaped curve.

In contrast, IPOs, very much up and down. I mean, part of the contribution to SPACs becoming very popular was that for a while, companies were not going public. So, that helped, you know, a lot, and then with respect to direct listings, there has been a lot of attention on direct listings, and it's a very unique structure and it's very interesting with a lot of benefits. But that -- you know, that really taken off as much popularity as you would think reading the media.

I mean, if you'd count the total number of direct listings, there has been less than 15 done, right, since Spotify did theirs in 2018. Spotify wasn't the first; it was just the first one done in the U.S. that was very, you know, well-known and got a lot of media attention.

So, that's kind of in a nutshell. If I have a few minutes, maybe I could just really quickly go through just the mechanics of each. And I know I'm a bit out of time, but I will try to go very quickly.

With an IPO, it's very easy, and, you know, everybody understands how an IPO works. A company will register an initial offering with the SEC and also apply to list the securities in the Exchange. They'll hire an underwriter to help them through the process.

The initial process just involves putting together a registration statement with the SEC -- register that offering -- and the first part of that registration statement, known as a prospectus, is the fancy offering document that gets sent to investors to market a deal.

The marketing the deal is done by the company and the underwriters undertaking what is known as a roadshow, where senior management of the company, along with their, you know, entourage of underwriters, at least pre-COVID, would go around flying to all the major financial centers, effectively, pitching the IPO and the company.

During that pitch, the underwriters would be taking -- will be building a book, which really just means taking down orders -- indications of interest. After the IPO process, the company and the banks -- the underwriters -- decide on a price. The price in the offering amount is formally offered to the company. If the company accept, the deal is deemed to be priced and the stock trades the next day on the Stock Exchange. So, that's a typical IPO.

There's one key feature -- you know, there are lot of key feature about it -- but one key feature that I'll mention is that in every single IPO, the underwriters will always seek to lock-up every single shareholder -- existing shareholder -- and the company from selling more securities within 180 days of the IPO.

That's partly to help the distribution to securities and maintain price stability, but it's also done to signal to the market that the company stands behind its stock -- its IPO. I mean, the investors, and the founders, and senior management all stand behind the IPO.

So, that's a core feature that I just mentioned because, you know, in contrast to direct listing. So, in direct listing it's very much -- it's very similar to an IPO in the sense that a company is registering an offering of securities and applying for the securities to be listed. But unlike an IPO, the company isn't marketing a block of securities.

Up to this point, all direct listings have just been the company, effectively, registering the resale of securities held by existing shareholders directly through the Stock Exchange. So, not to some initial investors that get the benefit of a public offering price, and then it trades, so ordinary people can then pull -- or institutions can buy on the Stock Exchange the next day.

With a direct listing, it's a direct sale through the Stock Exchange where buyers and sellers determine really much their own price. You don't really have an underwriting. You do have investment banks who are involved as financial advisors and they get paid some fee -- much less than an underwriting fee -- but by and large, it's just sellers -- existing shareholders selling and utilizing the registration statement directly through the Stock Exchange.

And, typically, it wouldn't be a lock-up, at least for most of the shareholders. Some of the recent ones have had lock-ups for key management, but they've been pretty bespoke and there hasn't really been -- or there hasn't been enough direct listings to really set a trend -- but my expectations will be that direct listings going forward would have some semblance of a lock-up.

And then the SPAC is -- and merging with a SPAC is where a private company merges with a public SPAC -- a SPAC that is done in IPO -- and the merger can take on a bunch of forms, but the traditional De-SPAC transaction involved a public SPAC dropping down on a subsidiary that then merges with a private company, with the private company as a survivor.

And so now you have the public SPAC on top of the private company as a combined company, and then the SPAC would just change its name and ticker to whatever the private company desired. Typically, it would just be the name of the private company.

There has been variance since then

where -- a big one now is for a private company that is foreign private issuer that wants to maintain that status -- in fact, being the one to survive and filing a registration statement -- typically an F-4 registration statement -- and acquiring the SPAC. So, that's a new variant, but fundamentally it's just a private company merging with a public SPAC and then becoming public companies through that route.

Those are the three ways -- and then with -- going public through merging with an operational company. Same as a SPAC except you have an operational company instead of a SPAC.

So, that's it in terms of just a kind of summary of the different pathways to go in public. Welcome any questions that anyone has.

MS. GARRETT: Thank you. I think what we'll do is we'll have each speaker just speak and introduce themselves and then we'll entertain the questions from the group.

So, our next speaker is Phyllis Newhouse. She's the Chief Executive Officer and a Director of Athena Technology Acquisition Corp., an all women-lead SPAC. While there are many active SPACs, only about three percent have a female chair or CEO.

Phyllis is also the founder and CEO of Extreme Solutions, a cybersecurity company with 6,500 employees globally. She was names Ernst & Young's Entrepreneur of the Year, and previously served in the United States Army with a focus on national security, where she established the cyber-espionage task force.

Welcome, Phyllis.

MS. NEWHOUSE: Thank you and thank you to the SEC for putting this on, and also the advisory team for taking time out to kind of hear our, you know, story today.

So, a couple of things I'd like to just really talk about. Number one, I'll tell you a little bit about my background. Number two, why I entered into this market, and number three, where I see the value add for SPACs, and the then four, really what I believe could be the future of SPACs.

So, just a little bit about my background. I spent 22 in the U.S. Army; ran the cyber-espionage center of the Pentagon before I retired, and actually today I have been retired 21 years. So, you know -- so, when I left the military, I knew I was going to be an entrepreneur.

I started the company primarily to focus and what I saw was a gap of - between private sector and the government, and really around national security as it pertains to -- or corporations, and governance, and compliance, and how we see cyber and how we see sharing information across domains. So, really that was our focus.

We've grown into what I believe is a very robust cyber organization that looks at many verticals of cyber concerns today, not just from the regulatory guideline, but, too, from -- you know, from just the individual use and how you use cyber, and just really what some of those risks are in terms of vulnerabilities as it pertains to our children and so on. So, there's a lot of different areas we're focusing on in the cyber with some of the cyber solutions that we've created.

So, as you stated, I started, you know, really thinking about SPACs. My company was -- you know, I'm going to give you this perspective -- so, about three years ago, SPACs started knocking on my door, and they started asking questions, and, you know, would I consider it. I really, you know, had an idea of what SPACs was, but really didn't understand really how -- how the vehicle worked as it pertains -- I understood direct marketing -- the direct listing; I understood how to -- the IPO process, but really not the SPAC process.

So -- and I will tell you, my experience of having so many different SPACs that I talk to, here's a couple of takeaways from that:

I saw SPACs that didn't -- where they didn't really understand the cyberspace; they didn't really understand the business model, and they really didn't understand really what the endgame was for the company as a publicly traded company. And so also I saw that there weren't really any SPACs that any women or minorities that I had spoken with.

So, you know, fast forward a couple years after that, I decided not to go the SPAC route of -- with any of the SPACs that had pursued us, us but I decided I wanted to be a part of a SPAC or potentially partner with someone to lead a SPAC, and that propelled me to meet Isabelle Freidheim, which -- through our organization, and we -- and then we decided --

Isabelle had already started to gather a team together and I came on as a CEO of the SPAC -- and here's what I believe why we entered the market -- because we saw an opportunity, number one, with the level of expertise and the network of women that we had. Our expertise spans across industry from, you know, to private equity world, to the venture world, to the banking -- investor banking, to the tech world, to founders, to operators, to creators.

So, we were very strategic in building a very diverse SPAC, but as the SPAC that we knew that differentiated itself from other SPACs. So, it was really based off of value-add SPAC on what you believed that we could bring to the market with the level of expertise that we had, but also to, how we can make an impact in the marketplace, so we did that.

And as we did that, we found that more companies were attracted to us, not because we were an all women lead SPAC, but because of the expertise that we had in the SPAC, and we were able to leverage that. And so I also looked at -- is that founders like to talk to founders.

When we had -- when I was being pursued by SPACs, I was talking to a lot of private equity hedge fund bankers and wasn't really talking to anybody that really understood the market, really understood the model, really understood the service offerings or the culture that we had created.

And so what Isabelle and I, as we built this team, we looked at -- those were the value-add things that we wanted to bring to the market. So, not only that, as a SPAC, we looked at the due diligence process.

Did we have third-party, very credible, tier 1, due diligence firms that we could strategically align ourselves with so that when we did find a target, that we weren't just taking a company to market just to have a transaction; that we knew that the company that we merged with, that this was a company that we knew was ready to be a publicly traded company -- not just the governance and compliance -- but had the ability to scale in the market, and that we could also use and deploy our expertise to help this company.

So, I honestly believe that by strategically putting together a SPAC with strategic partners, and putting the structure together, we would actually build -- have a SPAC that almost any company would want to De-SPAC with. And so where I see the future, yes, there's a lot of celebrity SPACs out there; there are people that will SPAC with their grandmother, as David said, or anybody for that matter.

But what I see is that, you're going to -- I believe that the SPAC market is going to change and you're going to see SPACs that are highly credible, have the expertise, not just from the financial, but, you know, you're starting to see a lot of CEOs who've sold, and acquired, and have many transactions under their belt that they can see the value that they can bring when you start bringing companies to the public market.

So, I honestly believe that SPACs are here to stay. I know that I intend to stay around and I believe that there's a lot of value that we bring. And so for the sake of time, I don't want to take more time -- so that we can get into a healthy discussion about this -- I'm going to say thank you.

MS. GARRETT: Thank you, Phyllis.

And our next speaker brings an academic perspective to this knowledgeable group. We have Michael Klausner, the Nancy and Charles Munger Professor of Business and Professor of Law from Stanford Law School, a place that's dead to my heart, and prior to becoming a professor in 1991, Michael worked as a corporate law practitioner and served as a White House fellow in the office Policy Development.

Mike recently published a paper titled "A Sober Look at SPACs", and we look forward to hearing his perspectives.

Mike.

MR. KLAUSNER: Okay. Thank you, Carla, and incidentally, if -- I've gotten a little bit of breaking up of the signal. I don't know whether it's me, or it was David initially, and then Phyllis. If it was me, interrupt me and I'll go to another room, probably with more dogs -- dog barking, but that would be better. So, just interrupt and tell me if you can't hear me.

Well, thank you, and thank you to the Committee. And Phyllis, as I said in our prep meeting, I think I'm going to agree with a lot of what you said, but it may not sound that way initially. So, give me a little time.

I'm going to share some slides and I don't use Webex typically, so I hope this doesn't get fouled up. Let's see if this succeeds. It says I am sharing PowerPoint. I have no idea what I just did. Let's see.

(Whereupon, a document was shared.)

MR. KLAUSNER: So, Carla, you're the person I think I have to talk to here. Do you see anything?

MS. DAVIS: It's Julie. I see your screen; I'm seeing your Chrome, not your PowerPoint.

MR. KLAUSNER: Okay. So, that didn't

work. If worse comes to worse, I can do this without -- you know, I see a thing that says "stop sharing". Let me try to share again.

MS. DAVIS: We can share them on this end if that would be helpful.

MR. KLAUSNER: Okay. Let's do that. Would it be -- yeah, why don't you do that. It's a little bit of --

MS. DAVIS: I actually have Jenny Riegel on our team is here to -- she bails me out all the time.

(Whereupon, a document was shared.)

MR. KLAUSNER: So, it's -- I see it -- it's small.

Okay. So, I guess it will be a little awkward. I'll have to tell you to keep advancing. So, why don't I say, whoever is controlling the slides, zip through all the line by line animation. I don't want to have to say "advance each line". So, when you get to a slide, just click a couple of times and see. It will be a little awkward, but we're a small group here I think.

Okay. So, what I'm going to be talking about is research that I've done on

SPACs that is still in a pre-publication draft, and I do have a draft that is almost ready as I go through the publication process, and I'll offer within a week or two, I'll be able to share that with the Committee and I will be putting it online as well.

The -- here's a picture of SPACs historically. They've done pretty poorly; in fact, they've done really poorly. These are returns; the downward bars are negative. Going from darker to lighter, they are, you know, one-week returns after the merger, one-year, two years. With respect to the last couple of years, of course, I can't get two years, but I use as much time as we have until now.

So, for 2020, you see initially SPACs did great in the first week. That reflects what I think was a SPAC bubble, and certainly appears to be a SPAC bubble in retrospect, but if we look at those same SPACs that merged in 2020, 2021, they're doing less well now as we come forward.

Okay. Next slide.

MS. RIEGEL: (Complying.)

MR. KLAUSNER: So, my question is why

do they perform so poorly. It's hard to find an asset class that performs so poorly consistently on average -- not Phyllis's -- on average. All this is averages -- means and medians -- and yet continues to survive. So, my research is an effort to look into that.

Next slide.

MS. RIEGEL: (Complying.)

MR. KLAUSNER: Okay. So, the root of it, I believe, and my co-authors believe, are the inherent costs built into SPACs. There's the sponsors' promote, which from the get-go is 20 percent of post-IPO equity. There are free warrants and free, you know, rights to post merger shares at -- a right is a right to get one tenth of a share at the time of the merger for free.

So, there's warrants and rights, which are issued in units in the IPO are dilutive. They come to a pre -- an initial cost of 11 percent of equity. Underwriting fee is 5.5 percent. There are other fees, which are almost a separate topic.

I find this astounding, how high the other fees are, but they're about four percent of equity and our total is about 35 percent of equity in costs out the door from the get-go when the investor puts in his or her $10 per share initially. So, David, I recommend that your grandmother not pick a random SPAC. Sounds like Phyllis's might be a good bet, but on average, its's not good.

We then move to the next stage that David has explained -- no, I'm sorry. You can stay back on the chart.

The middle column, there's a redemption right and then there's PIPE that comes in -- a private investment in public equity. So, there's money going out the door at the time a merger is proposed and there's money coming in the door when the merger is proposed.

And they -- you know, the magnitudes vary; there might be a net increase. There might be net decrease -- depends on the size of the PIPE and the amount of redemptions. During the bubble -- 50 percent.

During our study period -- which this is based on as you see -- is January 2019 to June 2020, redemptions were about what they are today. They were a little higher -- I expect redemptions may go a little bit higher still in the next few months, to go back to the norm, which is, in my view, you know, what we looked at in January '19 to June '20 -- January 2019 to June 2020.

And then post-merger, of course, you're -- all of this dilution is drawing a big company and post-merger dilution becomes a smaller fraction. So, you've got the numbers all there. Those are medians. The reason I use medians is because the means can make that middle -- they do make that middle column blow up a lot of because there's quite a lot of 90 percent plus redemptions. There's not a small number; 99 percent redemptions.

Okay. Next slide.

MS. RIEGEL: (Complying.)

MR. KLAUSNER: And you can click through the full side. I'll tell you when you can --

MS. RIEGEL: (Complying.)

MR. KLAUSNER: Okay. So, I want to now explain why redemptions amplify these costs I just put the screen. It's not just that money leaves the SPAC; it's that money leaves the SPAC and changes the ratio of cash in the SPAC to number of shares outstanding.

So, simple example, SPAC sells 80 shares in an IPO for $10 each and it gives 20 shares for free to the sponsor as a promote. So, initially the SPAC has $8 per share; people have paid $10 for those shares, but 20 percent is going out to the sponsor. Once again, if it's Phyllis, that may be money well spent. As you'll see, sometimes it is money well spent.

So, we've got $8 per cash, then the SPAC experiences 50 percent redemptions, so it now has $400 in cash. That 800 has shrunk to 400 and there are going to be 60 shares outstanding. All of the sponsor shares are still there and we've had a 50 percent drop in public shares. So, now those redemptions reduced cash in the SPAC on a per share basis to $6.67.

So, you can see, redemptions are roughly 50 percent today. I've just showed you how 50 percent redemption can pretty quickly get you down to $6.67 and we're only talking about the promote; we haven't even gotten to the overhang of the warrants, the cost of the underwriting, these other fees that come in.

Go to 75 percent redemption, and you can see where that story is going. Even down to $5 of cash per share that somebody has paid $10 for. Now PIPEs, we'll do the reverse. So, you can undo this with a PIPE and we'll talk about PIPEs in a moment.

So, next slide.

MS. RIEGEL: (Complying.)

MR. KLAUSNER: So, you know -- there you go, that's -- so, the mean is $5.70 per share -- you know, I may have that reversed. I'm going to have to take a look. I think I do.

The mean and the median are $5.70 in cash per share and $4.10 per share. One of those is mean; one of those is median. As I'm looking at, I think I may have it backwards. I apologize for that.

Once again, that -- those are not $10 a share because there has been a promote; there have been free warrants given out. There's sometimes free rights given out. The underwriter and other bankers, and to a lesser degree, lawyers, have come in and sucked more money out of the shareholders pockets, if you will.

Now, quick -- important qualification, we also differentiated in our study high quality sponsors from others. Now, we explain in the paper -- and I want to make clear here -- we defined "high quality" in a particular way that one can think of many other ways to define "high quality", and I expect that if you did, you'd get similar results to what we got.

But we defined it as a billion dollars -- if the sponsor is related to a fund with a billion dollars or more assets under management, or is a former CEO or CFO of a Fortune 500 company, we deem them "high quality" and we say in the paper, no insult to anybody who isn't one of those -- that doesn't mean they're "low quality".

We don't use that term; we just say "not high quality" -- but we find that defined this way, "high quality" sponsors have substantially less dilution than others, and one reason for that is they tend to have --

give out fewer warrants. The other reason is they tend to attract larger PIPEs.

Okay. Next slide.

MS. RIEGEL: (Complying.)

MR. KLAUSNER: Okay. So, who bears this cost? This is really an important question. The bottom line is going to be -- I'm going to explain to you -- that the shareholders bear these costs and that's reflected in the first slide I showed you. It depicts shareholders at the mean, at the median do quite poorly.

So, SPACs in a merger claim their worth $10; they're clearly not worth $10. They've $5.70 or $4.10, depending on the mean or the medium, per share of cash. Cash is the main -- the main asset that they're contributing to a merger.

Now, if you assume -- for this analysis, assume there is no other value than cash, and I put in parenthesis that this is debatable, and Phyllis just told you why it is debatable, because she and her colleagues expect that they're going to add value through their own skills, networks, business experience, etcetera. If that is true, then the analysis I'm going to give you in moment has to be changed to some degree. But let's assume that a SPAC is only contributing cash.

So, if the target were to treat the SPAC shares as worth $10 and say, "Hey, I'll give you $10 worth of my value", then what's going to happen is the target is going to bear that $4.30 cost; the difference between $10 and $5.70.

On the other hand, if the target looks at the SPAC, does its due diligence, says, "Hey, I see that you've got all these dilutive factors and I know there are going to be a ton of transaction costs by the time we finish with our financial advisors, etcetera. There's only going to be $5.70 of cash in this SPAC. So, I'll give you credit for that. I'll, in effect, in this merger, sell you my shares for $5.70". And if that happens, well then the SPAC shareholders will bear the $4.30 cost.

Okay. Next slide.

MS. RIEGEL: (Complying.)

MR. KLAUSNER: So, we did a simple

statistical analysis of the relationship between cash in the SPAC and post-merger share price, and what we found is that they're highly correlated.

For a small sample, which was 100 percent of the SPACs that merged in a yea-and-a-half, this was surprising. The more cash there is in a SPAC, the higher the post-merger share price, and the less cash, the less -- the lower the share price.

So, what this says is that highly diluted SPAC shares, or those with little cash in pre-merger, are going to have lower share prices post-merger. This shows up within a week; it shows up more dramatically, and statistically more significantly, in six months, and it continues to show up more significantly in 12 months, and you've got the picture there.

Now, I want to emphasize one -- two points as well. I've differentiated high quality from low quality. You see there that high quality SPACs tended to be -- to have less dilution -- more cash per share. I explained that. They also tended to do better, also consistent with what I said a moment ago.

The other thing is, one comment I often get is, "Hey, not all SPACs are bad", and of course, I agree. Take a look at the dot at the top. That's a good SPAC though it may be Nicola; I'm not quite sure. But there certainly are SPACs that have done well.

Okay. Next slide.

MS. RIEGEL: (Complying.)

MR. KLAUSNER: Okay. So, I think I've actually covered this to a degree when -- the question is, how do targets respond when they see a SPAC claiming in a merger agreement that their shares are worth $10 per share". They've got to overvalue themselves, so -- in effect, so they will generate a reciprocal overvaluation. That's our inference from the statistics and, you know, from some -- well let me leave it at that.

They will support their valuation by projections, which in separate research we have found to be exaggerated, more than bankers' projections in IPOs. So, they reciprocate by overvaluing themselves; they produce projections that support that valuation, and here is the second problematic aspect of the SPAC structure:

The sponsor and SPAC managers have strong incentives to go along with this, and as an aside, SPAC managers' interest, in general in SPACs, are highly tied to sponsor interest, not to -- not to public shareholder interests.

The next slide.

MS. RIEGEL: (Complying.)

MR. KLAUSNER: So, what are the SPAC sponsor and SPAC management incentives. They both want a good deal. If they can get a great deal, they both want it. That's terrific. But the sponsor and SPAC management will also take a bad deal. They got 20 percent of their shares for free; they own a big chunk of this.

If the shares drop in half, they're still going to come out ahead. On the other hand, if the SPAC doesn't find a merger partner, it has got to liquidate. If it liquidates, its 20 percent is worth zero and they have made an investment upfront as well of several million dollars; they will lose that.

That is, the structure of the SPAC provides that in a liquidation, sponsors get nothing, and all of the proceeds of the IPO are distributed to -- back to the shareholders -- the public shareholders, which is, as David said -- those funds are in trust, so they're completely safe.

So, this is where the -- emerge. The choice between a merger and a liquidation is not one with respect to which the sponsor and its management, on the one hand, and SPAC shareholders on the other up to degree.

Next slide.

(Whereupon, there was no response.)

MR. KLAUSNER: Can anybody hear me?

UNKNOWN SPEAKER: We hear you.

MR. KLAUSNER: So, I -- okay -- great. Okay.

MR. RIEGEL: (Complying.)

MR. KLAUSNER: Okay. Good. Here's the next slide.

So, here, I've shown market adjusted returns for a sample. I've truncated -- these are market adjusted, so you can go past 100 percent. That looked funny so we truncate that at 100 percent and you see that a few shares -- a few SPACs do well, but a large majority did poorly, and you also can see, once again, that the high quality sponsored SPACs, as I've defined that term, have done better than the other SPACs.

Next slide.

MS. RIEGEL: (Complying.)

MR. KLAUSNER: All right. So, we've been presenting -- the way the publication process works is there's a huge lag.

So, we posted our paper in pre-publication form about a year ago and we had presented it not a small number of times -- quite a large number of times -- and we've also gotten comments over the -- from a variety of people, and there actually have not been any substantive critiques.

We really -- in a way, we were hoping for it. Did we get something wrong? Did we calculate something wrong? But this is what we get from SPAC world. Your data is old. we started getting that response around October, November. Our data stopped in June. That is -- our data was three-months-old. We were told it was old. This time is different and this is as the bubble was inflating.

We got data -- we got responses saying, "No SPAC is like another. You're treating them all the same. Each SPAC is unique". Well, that's actually not true. "SPACs are constantly innovating"; not true. "SPACs are dynamic". SPACs have been the same since 2009 -- that the current version emerged, as David said, in 2009 -- they have been structured the same ever since; small changes along the way. Some potentially could matter, but they've been small and in small numbers of SPACs.

So, one of the surprising things to us in looking back over the past year is that so little has changed. Other comment we get is, "Let the market work". We agree with that. We have very modest policy recommendations and if you pick the next -- go to the next slide -- I think they are only two bullet points and I'll be finished --

MS. RIEGEL: (Complying.)

MR. KLAUSNER: -- we think that there should better, clearer disclosure pre-merger, net cash per share. By "net cash", I mean that it warrants end rights.

The numbers are there; you can find them, but I can tell you how -- it takes hours to decipherer this from the proxy. I'd like to see a chart that says, "You have put in $10" -- you don't even have to say that; they know they put in $10 -- "You now have $5.70 that we will -- we propose to invest in a company" -- and "we", as Phyllis said -- we believe we have the skills to make that $5.70 -- make up for the dilutive hole that has been created.

Just say that; let everybody know. Let them know that at the time. They can choose between going along with the merger and redeeming.

Second, I'm not necessarily opposed to projections in SPACs, but I think the rules should be the same for SPACs and IPOs. The cost projection -- the legal rules bias -- well, they more than bias -- they, in effect -- projections are absent in IPOs. They don't have to be, but they are absent as a matter of practice and they're always there or almost there for SPACs.

That's attributable to a safe harbor. I think that ought to be evened out so that we don't create that bias to drive, you know, companies into SPACs, which as I've said, are these highly dilutive vehicles, and I think that's all I've got.

MS. GARRETT: Great. Thank you very much, Michael.

And last, but definitely not least, I'd like to introduce Isabelle Freidheim. She and Phyllis are teamed up as Isabelle is the founder and Chairman of Athena's Board.

Isabelle is a venture capitalist and an entrepreneur with a track record of investing in disruptive technology companies. She most recently co-founded a fintech and artificial intelligence company, Magnifi, an investment platform powered by the only natural language search engine in the financial industry. Magnifi was acquired by Tifin in 2020.

Isabelle, thank you for joining us today.

MS. FREIDHEIM: Thank you and thank you to the Committee. I think the SEC is wise to explore the explosion of capital raised by SPAC sponsors and I think, generally speaking, the sponsor community welcomes the exploration process.

The increased attention to SPACs from the SEC, if it is directed towards enhanced disclosures, will benefit all investors, particularly retail investors, and will benefit the most serious SPAC sponsors, as you pointed out, like us, by leveling the playing field and making it clear to investors the high standards that we used, as Phyllis mentioned, to identify a target, diligence it, and ultimately get Board approval to combine with it.

As David mentioned, as of last week, there were 450 SPACs with over 130 billion in the market currently seeking a combination partner company. For historical context, SPAC IPO insurance had grown from 10 issuers, and roughly 1-and-a-half billion in 2013, to around 60 issuers and over 13 billion in 2019. Then the pandemic hit.

The pandemic highlighted four very important benefits of SPACs versus traditional IPOs, and those are first, the markets became extremely volatile, making the length required to come to market through an IPO excessively long in light of price and certainty.

Second, the trends underlying the digital transformation of our economy accelerated, creating a need for these companies to service our communities with their technologies, and in turn, accelerated their need for capital.

Third, it became clear to a universe of investors -- so, that's pension funds, endowments, growth equity investors, but also retail investors -- that -- as you pointed out this morning -- outsized returns have been achieved through the emergence of companies like Facebook, like Google, like Amazon, PayPal, Salesforce, Zoom. Well, those returns have been garnered by the venture community, which is a relatively exclusive community.

SPACs afforded a universe of investors the opportunity to build diversified portfolios and thoughtfully participate in this digital transformation trend.

And, fourth, by bringing companies to market earlier in the life cycle of the company, those companies were able to access capital to fuel their growth by providing projections. And SPACs have reinvigorated the public markets, and a result, SPAC issuance increased dramatically raising 83 billion in 2020 and 70 billion in Q1 alone of this year. But the market will dictate that because while in Q1 of this year, SPAC issuance was 70 billion, in Q2 and Q3 combined, that number is only roughly 20 billion and it won't increase by much in Q4.

Therefore, it is -- it is incorrect to say that nothing has changed. It is constantly changing. This year alone SPAC IPO issuance has declined by over 80 percent, and at the same time sponsor economics have compressed. The market is efficient.

So, the capital markets provide capital; capital is the life blood to innovation, progress, new jobs, and to our standard of living. Today, very importantly, many of the SPAC combination partner companies accelerate the technologies that fight disease and the perils of climate change.

Here are some companies that have gone public recently through a SPAC:

QuantumScape, the company that makes electric vehicles possible, over 200 percent growth; Heliogen, a company that we are taking public that replaces fossil fuels with renewable energy, and that head-on addresses the challenges of climate change.

There are many fintech companies that democratize access to finance, open lending for example, well north of 150 percent growth.

Virgin Galactic, as you mentioned, a company that aims to send anyone to space; Cerevel Therapeutics, 300 percent growth, a company that treats life threatening neuroscience diseases.

These are companies that would not have gone to market without a SPAC and they will be coming to us sooner because of SPACs. And to be clear, companies will succeed and companies will fail; the SEC plays a vital road in making sure that any investor, particular retail investors, understand the risks involved.

So, the question is, how do we address the concerns raised? Many of them are valid, but before we get there, let's remember two things.

First, let's not ignore that the markets are efficient. As you mentioned Michael, this was coming, and they do adjust constantly, but here's what I mean:

Ideal volume has dramatically gone down; as I mentioned earlier, 80 percent down this year after Q1, and the demand is just not there, and that has absolutely nothing to do with the warrant treatments -- I think everybody here knows that -- and has everything to do with the lack of investor demand.

Deals that have closed in the last couple of months have seen much lower valuations and better stock price performance. Why? Simply because either they could not raise a PIPE at the proposed valuation or they could not find a SPAC to merge with at the requested valuation.

We've seen increased volatility in the SPAC market. Retail investors don't like volatility, therefore, we're seeing significantly decreased retail participation and ownership because of volatility.

Sponsor economics are following the market; sponsors have recently started over-funding the trust to get IPOs done and that goes directly to protection -- from the downside at the expense of the sponsors who are being severely diluted. The sponsor economics are being compressed.

Second, let's not ignore that the demand is there. This morning we heard about crossover institutional investors into venture, but that's also true for retail investors who also wants the ability to co-invest alongside institutional investors.

I see this firsthand in Venn venture with where the retail investors trying to invest small check sizes in venture funds in pre-IPO deals and succeeds by pooling capital together.

There has been an increase in fintech companies that the market ties access by allowing retail investors to replicate trades and private investments made by institutional investors, and they view this as a privilege.

So, the demand is there and if

there are no outlets to provide the supply, those investors will continue to invest in unregulated private sectors that have significantly higher profiles -- risk profiles than SPACs do.

Of course, we don't want people to lose money because there won't be market participants anymore. We don't want everyone to be sued because then we carry too great of a risk of operating in this market. Therefore, I support every measure for increased transparency and disclosures, many of which were recommended by the Investment Committee.

Clearly stated rules for all constituents creates an efficient market. They help understand the risks; they help make informed judgments, and disclosures provide the level of rigor and due diligence, and level the playing fields and attract more serious sponsors, and they raise the standards that we want other sponsors to live by.

So, more specifically, disclosures that relate to the qualifications of SPAC sponsors to evaluate a target, the compensation structures of all constituents, the potential conflicts of interest that do exist, as they do in many other investments, the mechanisms and the economics explained in a visual manner through diagrams, those are probably the most helpful.

Professor Klausner suggested disclosing the pre-merger net cash per share. That's fine, but even more importantly, disclose the actual price paid by the sponsor for the company that includes the promotes. Disclose the crucial due diligence that has been performed and disclose how the valuation was performed.

That being said, I think the SEC and Congress should be -- should think very carefully and cautiously about curtailing a SPAC's ability to provide financial projections for combination partners, because doing so would preclude these companies from accessing the public equity capital markets for years.

It would slow their ability to bring their innovations to our communities, as it increases the development of time due to the lack of availability to fund, and thus increases time to market for companies making a positive difference in our world.

Likewise, it has been suggested to imply -- to impose regulatory curtailments of sponsor economics. That would harm the capital markets and the efficiency by which capital flows to the best ideas and the best innovations, the best returns, and pulls back from the worst. Using that logic, last year the top 10 people were -- top 10 paid people in finance were hedge fund managers.

So, let's regulate their cared interest and cap it at 10 percent or let's create caps on the compensation of other functions.

Who decides the cap and how do we start setting caps for all joint functions because where do you draw the regulatory line? How much is the most a lumberjack should make, or how is the most a doctor should make, or how about a nurse, or is it that every function in America is appropriately priced except this one?

If you go down that road, you create a precedent, which is in direct contradiction to a free market concept that has made this country great. The Unites States is the most advanced, innovative, hardworking, and generous nation in the word. It is the land of opportunity.

A major reason our capital markets are the most efficient in the world, they're trusted, and the more transparency, the better. However, creating the precedent of government working groups that determine the economic contribution of each function in society would undermine the foundation upon which we have gained our standing on the world stage.

So, a transparent and liquid capital market is a good thing -- it's actually a great thing. It has been the life blood to the economy with the greatest innovation, and SPACs play an important role and we should ensure that it continues to provide great companies another choice to access the public equity capital markets.

Clearly, in light of the speed for which they have become one of the principal means by which founders and innovators consider accessing capital, it is wise, indeed, to ensure the requisite transparency and disclosures are enforced.

So, I appreciate the opportunity to speak on behalf of the sponsor community and as a proud American.

MR. SOLOMON: Well, thank you Isabelle, and thank you, everybody, for sharing these.

You know, it has been a phenomenal afternoon session so far with lots of different views and lots of information. I wanted to take the time now to open it up to Committee members to ask questions. If you have one, please put it into the chat, or if you want to actually just let us know, we can call on you in an organized fashion.

MR. NI: Yes, I'm sorry, Jeffrey. I's David. May I just add a comment just to help set a context here?

So, the focus here is on small business. I think -- look, direct listings, there has only been 15 and they don't really work for small companies. In fact, they don't work for, you know, 90 percent of the big companies.

So, it -- you know, I'm happy to

entertain questions on that front, but I do want to highlight that.

But another thing I wanted to highlight, since there's so much focus and interest in SPAC, is just to point out that as of two weeks ago -- you know, this topic may be irrelevant for small companies -- because the SEC's Office of Chief Accountant staff has put out guidance that would effectively eliminate small SPACs, like, you know, the 50 million range.

That would be, you know, within the realm of possible for smaller companies.

It would just, effectively, eliminate on a going forward basis because it would prevent listing at the Nasdaq's lowest tier market, which allows for 50 million dollar SPACs -- 60 million dollar SPAC -- it would mean that going forward, unless there are some changes, that smaller SPAC will be 75 million dollars, which if you -- if you generally apply the rule of the thumb that is SPAC, because of dilution purposes -- cannot or will not merge with a company that is, you know, smaller than three or four times the size of the trust value.

It means that, effectively, SPACs will only be available for companies that are around at least 300 million dollars or more.

So. I just wanted to highlight that for the team, just cause I know we were jumping deep into SPACs.

MS. NEWHOUSE: And if I could just add one thing to what you're saying about the small business, I think it's -- even a small business going any route -- any -- whether it's direct route, or whether it's IPO, or whether it's through a SPAC -- and this goes back to the quality of SPACs, understanding the due diligence process that has to take place in order for a small business -- even some large companies have difficulty meeting the governance in compliance around being a publicly traded company, and small businesses that mature -- that get their process matured to a point to where they can go public, that they do have the infrastructure in place, and that a SPAC has the expertise to see that as well.

So, even in the smaller SPACs, I

think, struggle with if the company has the public readiness as well.

MR. SOLOMON: Thank you. That is -- so, two very important point here that I think are critical for us to consider.

I want to -- Kesha, you have a question -- or Kesha -- sorry.

MS. CASH: Yeah, no, thanks, Jeff.

Hi -- I wanted to say hi to Isabelle.

We attended Columbia Business School together and we're part of the Columbia Student Leadership and Ethics Board. So, it's great to see you and to hear from you.

Building on your note and point about some of the ESG focused companies that have gone public via, you know, a SPAC, can you talk a bit more about -- you made the comment, these are companies that would not have been able to access the public market otherwise, and Phyllis's point around value-add -- can you give some more specifics around that value at -- via a SPAC versus otherwise not being able to access the public market?

MS. FREIDHEIM: To go public through

an IPO, SPACs -- companies need to present -- cannot present projections.

To go public through a SPAC -- and it has been one of the most touted benefits of SPACs -- you're allowed to present projections as the company to the management team. The management team will believe them or not. As sponsors become better qualified and as sponsor groups become better able to evaluate companies, they're better able to assess the quality of those projections.

So, companies don't have the option -- so, companies that are much earlier staged don't have the option to go public through an IPO. In many cases, they don't have revenues -- some are ESQ; some are from other sectors -- and that ability to go public through -- to go public all together also gives companies, by the way, access to the public company premiums.

So, with regards to Professor Klausner, your point about the dilution that the company is willing to pay for it to go public through a SPAC, SPACs are willing to pay for, well, one obviously the time. FedEx has made an entire business around the concept of the value of time, but also SPACs are able to benefit from the public company premium.

Take the same company, make it a public company versus a private company, you get a significant public company premium, and from that SPACs are able to partially cover the sponsor dilution.

MS. NEWHOUSE: And I'll just say this, from the value-add of the expertise, if a company is -- in my case, as a cyber company, looking to go public, if I had gone through a SPAC, the number one thing that I was looking at was did they have the expertise.

I would be willing to take that dilution if that was a company that I knew, or a SPAC that I knew, that had the expertise and understood the market, understood the business, and was willing to roll their sleeves up.

So, I look at SPACs and say, you have either your transactional or your relational and transactional because it's not -- to me, it's not just okay to say, "We just want to do a SPAC and De-SPAC for this company", and you don't have the intentions of making it a great public traded company.

So, really, I think, in our case, it was, if I look at what we're doing to help the company that we -- that we're De-SPAC'ing with, you know, we're deploying the expertise that we have from cyber, to the strong technical expertise, to the -- you know, the financial expertise that we have on the team from being involved heavily with the company as they're going through this process.

So, it wasn't just a transaction for us, and I think that that is what separates or differentiates a lot of the SPACs -- the high quality SPACs that he spoke about early -- earlier -- I think the high quality SPACs have great intentions of seeing that company really be a great publicly traded company. And not just that, but seeing the investors get a return on their investment as well.

MS. FREIDHEIM: So, the bottom line, Kesha, is just, it's just not an option for many of those tech companies who are earlier staged to go public through an IPO, and so -- and these are covered by the safer harbor concept -- so, by not giving the benefits of the safe harbor to SPACs as well, you're not -- you're not allowing to present protections.

So, you're cutting off access to what is an important supply of capital to companies that need it to bring their value to our communities.

Over the last couple of decades, by the way, the number of public companies that have access to public capital has shrunk from almost 8,000 down to 4 or 5,000. So, we've been going the wrong way. We -- if we want to give all Americans the opportunity to share their ideas and participate in that wealth creation, we shouldn't further consolidate power in fewer corporations, rather make a U-turn and embrace new innovators.

If you remove the ability to provide projections, you're hurting companies' ability to help us and that exacerbates climate change. It slows health care innovation; it forces innovators to access public equity through the traditional funnel of Wall Street investment banks who are very valued, but just to be clear, not exactly known for their diversity and inclusion.

So, you're relegating those inclusion decisions to them.

MR. SOLOMON: So, just to be clear, I think what Michael -- and Michael, you can certainly speak for yourself -- but I think the comment was really to balance it out so that maybe, you know, if it wasn't necessarily just eliminating projections for SPACs, it may be allowing projections as part of an IPO process. There is a regulatory change that would have to be made in order for that to happen.

There's a reason why projections are not included in IPOs. That has to do with underwriters not wanting to be held accountable for validating those projections. That standard does not exist in SPACs today, so I think this is a technical matter, but it's a very important distinction.

It's not that underwriters or companies wouldn't want to include their projections in IPO; they really aren't being allowed because of the underwriter's liability associated with those projections.

And so that same standard is not currently being applied in SPACs, and so that's why SPAC mergers, which actually -- it's actually a public company technically goes public through a merger proxy as opposed to a prospectus, and that merger proxy actually mandates that you actually have to put projections in as part of the rules around mergers.

So, that disparity is a technical disparity, but it's a very really one, I think, as Isabelle has highlighted, cause it enables earlier stage companies to allow -- to put their own management projections out there, which investors can spend a lot of time with and decide on their own if they really like them.

So, I just wanted to clarify that for the Committee, and, Michael, I don't know if you had a -- if you -- I didn't mean -- I didn't know that you -- I didn't necessarily think you were implying we should take projections out of SPACs; I think you were saying maybe it could be a little bit more balanced in that regard.

Is that correct?

MR. KLAUSNER: Yeah, I'm glad this is

being recorded cause I said, I am not opposed to projections. I think that the bias -- the legal bias towards SPACs is a very high price to pay to get projections, so allow them in IPOs as well.

Now, as John Coates, when he was Acting Director of Corporate Finance said, perhaps more disclosure should be provided around those projections -- around the basis for those projections. I have a fear that that's going to become the same boilerplate that we now have around projections, but, nonetheless, there's no justification whatsoever for allow -- for having a different legal rule in SPACs versus IPO.

It's entirely backward because SPACs have these high transaction and dilution costs built into them. It's too high a price to pay for an arbitrary -- arbitrarily different legal treatment.

So --

MS. NEWHOUSE: Michael, let me --

MR. SOLOMON: I just want to make sure -- there are a few more questions and we'll get back to dilution and cost in just a second.

But, Sara, you had a question.

MS. HANKS: Yeah, this is sort of more of a comment, which is, you know, I'm struck by the fact that, especially coming from small companies, which is what I work with, it seems to me like the very existence of SPACs -- this weird Rube Goldberg structure -- is an indictment on the complexity of going and being a public company, and shouldn't we really not be focusing on how to make SPACs better, but to address the issue of why SPACs exist in the first place, which is it's really difficult to become a public company. Why can't we just make it easier to become public companies in the first place and then we wouldn't need to do all of this stuff.

And then, of course, my friends at the SEC will not be surprised -- I say this all the time -- why can't Reg A companies be public companies?

Why can't we use Reg A as the structure for being a publicly traded public company on the basis of the disclosure required under Reg A?

MS. FREIDHEIM: And that's a very good

point, Sara, and hopefully, it goes the other way in the direction of allowing projections in an IPO, rather not extending underwriters' likability to the De-SPAC in SPACs because I did see that mentioned in the Investment Committee's suggestions. That is not a good idea.

MS. HANKS: I'm just in favor of Reg A, that the -- the liability standards slightly different, possibly more appealing to everybody.

MR. SOLOMON: Thank you, Sara.

Bert, you had a comment?

MR. FOX: Yeah, really two. I mean, I -- the first comment is, is I do think that this liability issue is something that needs to be looked into and I think it goes both ways.

I totally understand the comments about the projections being helpful and I do wonder if what we're seeing is maybe not an indictment of the entire going public process, but similar to how biotechs and stuff have evolved into an ecosystem that has a lot of public -- early public offerings to fund them if some of these, you know, low revenue heavy capital intensive industries are -- need some sort of similar ecosystem, that we're seeing the beginning of that.

But I think this liability issue is a huge one because, you know, while I understand the people with good interests are -- you know, heart -- would have -- these projections are helpful, but it also seems very ripe for abuse as well and I am worried about some of the investor projections involved with that, and so that's my first comment.

And my second one is maybe a question for the professor. When you talk about the high quality sponsors -- cause I will say, when I've been looking at this and my firm auditing some of these sponsor SPACs, which is a newer thing for us, it does seem like the thing that is different this time is the high quality and level of sponsors that actually are involved to the past, and I don't know if your research backs that up or not.

MR. KLAUSNER: Yeah -- yes -- yes. It has been reported that there are more high quality sponsors. On the other hand, there are 400 and some SPACs outs there now.

So, we did not collect data since our sample period, or since our study period, to see whether the proportion of high quality sponsors is different. So, I can't answer that question, but we did find that high quality sponsors did better than others and so, you know, the more the better.

There still are plenty that are not high quality; I can tell you that.

MS. NEWHOUSE: Michael, can I ask --

MR. SOLOMON: Phyllis --

MS. NEWHOUSE: Can I ask -- can I ask, in your percentage of quality SPACs, what percentage of those were women and then what percentage were people of color? Just curious.

MR. KLAUSNER: I didn't collect data on that, so I don't know.

MS. NEWHOUSE: Okay.

MR. SOLOMON: Phyllis, I know that you had another comment that you wanted to make earlier and I think I might have cut you off by accidental.

MS. NEWHOUSE: Yeah, it was around the projections and, you know, I guess it was more of a comment.

I know that a lot of SPACs are doing Fairness of Opinions to support where they're coming up with the projections and I also think -- I know in our SPAC, it was important for us to have, again, the third-party due diligence to make sure that we were looking at, you know, this from a total different perspective that what we were seeing internally to make sure that externally, our external partners saw the same thing that we were seeing in this company.

So, I don't if you're seeing a lot of SPACs do the Fairness of Opinion; was that something that's going to be required in the future?

MR. NI: Yeah, I mean, I can give you the practitioner's perspective and I -- we still don't see most SPACs due Fairness Opinions generally. You know, every SPAC will commit to do a Fairness Opinion if they're going to engage in a De-SPAC with an affiliate or if there are other facts that may warrant it, but the vast majority of SPACs still don't do any Fairness Opinions or engage, like a Deloitte, in helping them with financial diligence.

I think there might be a small shift though -- I mean, not enough for me to be certain, but, you know, there's certain of our clients that we're working with who, largely in response to the Momentus case, which is, you know, that SPAC -- it's the -- acquisition SPAC that got dinged by the SEC, even before it went effective.

So, a lot of -- some of our smaller -- especially smaller clients who, you know, don't feel like they have the technical sophistication to do as robust a diligence as some of the bigger players, they are inquiring about whether they can be more protective by hiring somebody to do a Fairness Opinion or hiring -- or loading up on third-party specialists.

So, it's kind of having that affect, but, personally, I am not seeing a trend towards more Fairness Opinions from -- you know, by any De-SPAC that doesn't involve an affiliate.

MR. SOLOMON: So --

MR. KLAUSNER: -- directors -- how

many do you see that are truly independent? I see a lot that are really not at all independent.

MR. NI: Well, the vast -- well, so there's several ways to answer that. I mean, technically, if you -- among pretty much all the SPAC IPOs I've looked at or worked at, right, the invest -- the underwriters will always advise the company, you have to have a majority of independent directors.

You don't have to because most of these SPACs are structured so that the SPAC is a controlled company under the Stock Exchange Rule, so they can get away with not having a majority.

The general advice is, you need to have majority independent directors cause investors are going to care about that. It's going to make your life, from a liability perspective, easier, and then too, you need to have proper management.

So, I think in my experience anyway, I mean, among the SPAC Boards I've looked at -- and I haven't done a broad survey -- generally, that there are a majority of independent directors.

How independent are they? I mean, are they truly free from, you know, relationships that would make them truly independent? I can't answer that.

All I can say is they do -- you know, you have to meet the Stock Exchange independent requirements and if you're on the Audit Committee, you also have to meet the SEC Audit Committee Independent Requirements.

But, you know, I would also tell you that every SPAC asks with a control company, can we just -- you know, can we have three insiders and two independents, and, you know, the underwriter always says, "No, you can't have that because that will impact investor perception of you as a SPAC".

MR. KLAUSNER: My impressions are there are a lot that are not independent and more than that, are functionally not independent because they have -- their compensation is in sponsor shares and founder shares.

So, their economic incentives are aligned with sponsors, not with public shareholders. They're not giving the public shares.

MR. SOLOMON: Yeah, there's a couple of things on that front and I want to make sure that we clarify for the Committee a few things.

This is -- I can't believe we're actually talking about this at a Committee meeting.

As somebody who has been around the SPAC market for a long, it's just -- it's still odd to me that the SPAC market has grown up so quickly that it merits a lengthy discussion, but it does because of all the reasons, I think, that everyone highlighted today in the size and the impact that it's having on the industry.

Two things: First of all, I think there's a -- we need to draw a distinction between the SPAC IPO and then the subsequent, what we call, either De-SPAC or the post-merger, effectively, IPO. They are two very different things and when the conversation that was just being had between David and Michael, was really a focus on the initial IPO.

And I think it's important for the

Committee to recognize that in an initial IPO, the -- every investor, individual institution, every investor in the initial IPO has a redemption right upon the announcement of a deal.

So, that money is -- Professor Klausner had highlighted -- is segregated and it is put in trust, and when a deal gets announced, if any investor -- again, individual or institution -- doesn't want to participate in the company going forward, they put in redemption right and they get all their money back, plus a small return, and that's -- nothing we've talked about here. You know, I think -- I don't think there's any disagreement around that.

Most of the debate and the discussion that we're having is what happens when a SPAC announces a transaction, and what are the implications around announcing that traction action, and how will be economics flow from that point going forward, and I just think it's an important distinction that perhaps we glossed over.

That's really what we're talking

about here, is the De-SPAC transaction, and I think there's some mis-impressions around that and -- that -- and there's just -- because it's a very complicated area, a lot of the suggestions here around increased disclosures, plain English disclosures, allowing every investor or to see where the economics fall, are really, really going to be critical elements of the development of this ecosystem if it continues -- as it continues to mature.

And I just don't a lot of people paid attention to it before because it wasn't big enough for anybody to pay attention to, and now it is, and so it's -- I think, as everybody has rightly pointed out -- time for us to actually think about ways to make that disclosure more transparent so that there's a more level playing field.

Andrea, you had a question.

MS. SEIDT: Yes, thank you.

I wanted to get back to projections a little bit. I had a question for Michael.

In the state regulatory space when we look at private and exempt offerings, we see a lot of abuse with projections. They definitely are -- get deals sold to investors, but there's a lot of confusion. A lot of the times those projections are not realistic; they're not grounded in fact, and they are never attained down the road.

And so I wanted to know, Michael, when you were sharing some of the historic returns on SPACs, whether you have done or whether you're aware of any other research that has been done, to validate or test projections on the SPAC space. So, it would be very interesting to see what the SPACs that you have been able to assess returns, what they were in fact projecting for investors.

Have you done that research or are you aware of anyone else doing that kind of research?

MR. KLAUSNER: Good question. Funny you should ask.

We are currently doing that research. It's very time consuming, as was the initial research. Preliminarily, we are finding that -- I think I mentioned -- that SPAC projections are overly optimistic; they are not met.

They are not infrequently guided downward after the merger and that when we -- again, this is preliminary -- we compare that to bankers' projections in IPOs. SPACs are worse.

So, we -- I can't tell you what the conclusion of the paper is going to be, but as we're collecting data, and we're collecting it, you know, as we speak, it came back; we've got some more research assistants helping us. We will have that and that's where it stands today.

Now, I mean, again, it's built in though; The overvaluation of the target is built in to the overvaluation of the SPAC. So, this is very complicated to untangle, but let me stop there.

MR. SOLOMON: Yeah, I also think it's worth noting -- and then we're going to go to Kesha in a sec -- it's also worth noting that when calculated, there's a lot of debate over how to calculate delusion in these, and I think the press have laid out one way in particular.

But certainly because there's a

reset and every investor gets the chance to make a decision on the ownership structure -- the new ownership structure is basically a merger between -- where there's a valuation for the private company and a valuation that gets delivered on the part of the SPAC.

And so it's easy to say 20 percent because that's what it appears nominally; it oftentimes is not that number, and it varies depending on how much cash remains in trust or how much cash does not remain in trust.

And, of course, it's only recently in the two-and-a-half decades of SPACs that sponsors have actually been able to keep 100 percent of their sponsor shares. Up until pretty much 2019, despite -- every sponsor had to negotiate away a lot of their sponsor shares in order to get transactions done.

So, there's a lot of stuff that goes on towards the end of the SPAC transaction, which makes it more complicated, I think, to make -- to draw a broad conclusion. Having said that, again, it gets back to there should be adequate disclosure prior to the closing of a transaction so that every investor has equal access to information to make the decision of whether or not to stay in or to redeem.

MR. KLAUSNER: Just to be clear, our numbers in the second -- second and third column reflect the compromises that sponsor made in its promote in the merger. So, we incorporate that.

It starts out at 20 percent; it tends actually not to drop by very much. That is before the bubble. During the bubble, it may not have dropped at all. I don't recall, and earn-outs is another thing we can talk about -- another study I'm doing. Little complicated, but far less there than meets the eye.

MR. SOLOMON: Kesha.

MS. CASH: I want to ask the -- maybe the obvious question, but don't want to overlook the fact that we have here women and people of color that have launched a SPAC, which I think is rare in the SPAC world, and Phyllis, you had asked about the diversity metrics.

So, I'd love to hear, Isabelle and Phyllis, from you two, any challenges you had as women and people of color launching your SPAC and how you -- and I kind of -- I heard it through some your conversation, Isabelle -- but how do you -- what do you believe or how do you believe SPACs can democratize access for marginalized groups in America.

MS. FREIDHEIM: Phyllis, you take that.

MS. NEWHOUSE: I knew she was going to say that, but I'll say this, when we did the SPAC, Isabelle and I looked at the numbers across the board and there were -- there had not been any women of color leading SPACs, and then we looked at the number of women on management teams in SPACs. That number was very, very small.

We looked at the number of women that were sponsoring SPACs and we could only find one woman that was actually sponsoring other SPACs, and that had done more than one SPAC -- that had been a repeater back to the market. The numbers were small.

And so when you look at this as a whole, women of color, that number was -- didn't even exist, and so when Isabelle and I were even like doing something on the IPO raise, when we talked to investors, we rarely saw -- there were no people of color; there were only one -- I think one woman.

But here's what we found, is that when we talked to the investors, it was very few investors that actually said, "Oh, you're an all women led team". They looked at the expertise that spans across industries; they looked at the backgrounds, the Board, the -- and what we got was, "Wow, what you guys put together, one hell of a team".

And I think when we went to market, there were a lot of companies that loved the idea that we were so diverse with diverse backgrounds.

We had -- again, we had the expertise across the industry.

So, we -- although there are challenges with any SPAC, I believe, but I think we had the expertise based off our backgrounds.

I mean, heck, I spent 22 years in the military, so there's probably not an industry that I wouldn't tackle after spending

22 years in the Army.

And so I think for Isabelle and I, we saw the challenges, but we also knew that we had to -- we had to overcome that and we had to get there that.

And so I believe that you're going to see more women now come into this market, and embrace this market, and know that it still will not come without challenges, but they've seen women that have had successful transaction and they'll follow. That's what I honestly believe.

MR. SOLOMON: Thank you for that commentary and thank you to everybody really for sharing this. It's a great beginning of discussions more to come. I think it was -- for us, it was a very big day of learning and that's super helpful.

So, I'm going to turn it back to Carla because we're getting up on time here and I want to make sure that we -- that we let everyone go on time.

So, Carla.

MS. GARRETT: Yes, I just want to thank everybody for their participation today.

As Jeff mentioned, I think this was a great introduction to topics that I'm sure we will discuss in future meetings.

Just to remind people, our next meeting is on November 16th and unfortunately as a result of the ongoing pandemic, it will be remote again, but we will look forward to seeing people on the 16th and thank you presenters, thank you panelists, thank you Committee members.

And I hope everybody has a terrific day, and I hereby adjourn the meeting.

(Whereupon, at 2:28 p.m., the examination was concluded.)

* * * * *

PROOFREADER'S CERTIFICATE

In The Matter of: SMALL BUSINESS CAPITAL FORMATION ADVISORY COMMITTEE
Date: Monday, September 27, 2021
Location: Washington, D.C.

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

_______________________ _______________________

(Proofreader's Name) 10-4-2021

C E R T I F I C A T E

STATE OF NEW YORK)
:SS
COUNTY OF NASSAU)

I, Julia M. Speros, a Notary Public within and for the State of New York, do hereby certify:

I reported the proceedings in the within-entitled matter, and that the within transcript is a true record of such proceedings to the best of my ability.

I further certify that I am not related to any of the parties to this action by blood or marriage; and that I am in no way interested in the outcome of this matter.

IN WITNESS WHEREOF, I have hereunto set my hand this 27th day of September, 2021.