U.S. SECURITIES AND EXCHANGE COMMISSION

MEETING OF THE SEC SMALL BUSINESS

CAPITAL FORMATION ADVISORY COMMITTEE

Tuesday, November 12, 2019

9:37 a.m.

U.S. Securities and Exchange Commission

100 F Street, N.E.

Washington, D.C.

PARTICIPANTS:
Jay Clayton, Chairman
Hester Peirce, Commissioner
Carla Garret
Jeffrey Solomon, via phone
Sara Hanks
Youngro Lee
Brian Levey
Sapna Mehta
Karen Mills
Catherine Mott
Poorvi Patodia, via phone
Jason Seats
Hank Torbert
Gary Yadley
Martha Legg Miller
Greg Dean
Mike Pieciak
Mark Sharma
Collin Caleb
Jenny Riegel
Jessica McKinney
Rick Fleming

SPEAKERS:
Ross Baird
Richard Horowitz
John Finley

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PROCEEDINGS

MS. GARRETT: Good morning. I hereby call the meeting of the Small Business Capital Formation Advisory Committee Meeting to order. I am Carla Garrett, the Chair of the Committee. And via webcast, I believe we have Jeff Solomon, the Vice Chair of the Committee. I believe we also have the following committee members who are participating via phone or webcast. As I said, Jeff, Steve Graham, and Poorvi Patodia, excuse me, sorry.

MS. PATODIA: Hey, there. This is Poorvi Patodia. I'm here.

MS. GARRETT: Is Karen Mills on? Okay. Julie, is there a quorum for the meeting?

MS. DAVIS: Yes, there is.

MS. GARRETT: We would like to thank also Terry McNew for his service on the committee. Terry is no longer on the committee because he has left MasterCraft Boats and he has joined Klaussner Furniture as their new president and CEO, but we would like to thank Terry for all of his time on the committee.

Thank you to the members of the committee and the SEC staff in attendance. I welcome the people attending the meeting in person and the viewers via webcast.

Today we will be discussing and possibly making recommendations on the SEC's Harmonization Release. The goal for the meeting today is for the committee to be a source of original thought from the perspective of how to facilitate capital formation for small businesses. As director Hinman stated in our August meeting, the SEC would like this committee's input both at the high level of addressing the exempt offering framework as a whole, and at the detailed level by making recommendations on discreet areas of the release.

Today's agenda will be as follows: First we will have a guest speaker that will talk about how small companies are assessing capital at a company's early stage. Next, the committee will discuss the Harmonization Release and will work to develop possible recommendations. After lunch the SEC Investor Advocate will provide an introduction to the Office of the Investor Advocate. We will then have two guest speakers that will provide background on ways to facilitate capital formation and exempt offerings through pooled investment funds, which could provide retail investors with greater access to private growth stage companies. And following these speakers, the committee will continue its discussion on the Harmonization Release and

deliberate on potential recommendations.

I'd like to turn the meeting over to Martha Legg Miller, the SEC's advocate for Small Business Capital Formation, for more introductions.

MS. MILLER: Thank you everyone and I appreciate everyone being here today with what sounds like lovely weather and some metro delays, so I know that we have one, our speaker Ross Baird, who will be joining us as soon as he can.

I did want to start with something that I've really appreciated, the number of our advisory committee members who have reached out after the meetings and touched based to share thoughts and ways that we can be an even stronger group.

One of the things that was raised by one of our committee members was a discussion of first principles to ground us, and the discussion of how we approach and think about the issues. And so I just thought I would take two minutes to briefly kind of take a step back and remind everyone of kind of the enabling legislation and what the thought process was behind the creation of this committee is just something to ground us as we look at topics today that can go down many different rabbit holes and take on a lot of different perspectives, and that was that Congress wanted to

create an advisory group that could think strategically about the encompassing issues of the marketplace from small companies that are start-ups and very early stage in emerging, and across their life trajectory all the way up into small cap public companies, and thinking about how we can approach that from a perspective that balances the needs of companies and investors, but that is looking holistically and prioritizing that entire pipeline and trajectory for growth.

And so with that, I think it's a helpful framework for thinking about the issues, thinking about holistically what enables the emergence of new marketplace entrants to grow and thrive and scale as meets their needs. And if anybody has any additional further thoughts they wanted to add in about legislative history, there is a good bit that is out there, but hopefully that's helpful as just a grounding first notion, and I appreciate the recommendation to start with that.

MS. GARRETT: And Martha, did you want to introduce Chairman Clayton?

MS. MILLER: Yes, I am happy to introduce Chairman Clayton. And before I do it, I will also give the lovely disclaimer that we give at everything you come to with the SEC, which is when any of us are

speaking, we are representing our own perspectives, not necessarily the views of the organizations we represent, whether that is the Commission or your respective companies, which is a good omnibus disclaimer that can get us scot-free out of having to do that for the rest of the day.

And with that, Chairman Clayton, we appreciate you being here today to kick things off.

CHAIRMAN CLAYTON: Thanks, Martha, and thank you, Carla. It's nice to join all of you today, and I want to recognize that you all have day jobs, busy day jobs, hard day jobs, and we greatly appreciate that you are lending your time, your limited time to help us with these issues. And it's very important because you are the boots on the ground. You are the people who actually have to navigate our markets and our laws to try and get things done. It's fairly easy to sit up here and talk about how great things can be and whatnot, but when you're doing it every day, it gives you a tangible insight, and I can tell you that that tangible insight is very important to us. So I'm pleased that you will devote today's meeting to a discussion of our concept release on Harmonization of Securities Offering Exemptions.

Taking a critical look at our offering

exemptions is important for investors and issuers alike. Are they working? I believe that our private markets are not providing opportunities to our Main Street investors to the same extent, including quality, they provide to our institutional investors. Our markets are far different today than they were 35 or more years ago. Then, our private capital markets were a minor component of our economy for both companies and investors. Today, in terms of the amount of capital raised, investment opportunities, returns, and other key metrics, our private capital markets often are seen as more attractive for companies and professional investors than our public markets.

However, our overly complex and rigid approach to private offering regulation was built on a patchwork basis for the markets of 35 years ago. This approach focuses on direct access and it is rooted in investor protection concerns that, to be sure, let's repeat this, to be sure must be respected and furthered. However, I believe it is an overly reliant system on the wealth-based definition of accredited investor and it effectively prohibits or significantly restricts all but our wealthiest Main Street investors from investing directly or indirectly in our private markets. Worse, because the costs of providing access to Main Street

investors on an individual by individual basis, including those who are very wealthy and qualify as accredited investors are high, those seeking to raise capital in the private markets generally may turn to our Main Street investors only if institutional investors are not sufficiently interested. Said another way, the way economists would talk about it, there may be significant selection bias that adversely affects Main Street investors.

For these and other reasons, I believe it is our obligation to explore whether we can reduce costs and complexity and increase opportunity for our Main Street investors in this important market, including through professionally managed funds. To be more specific, I'm thinking about funds where Main Street investors are able to invest in the private markets on terms similar to those available to institutional investors and on a diversified basis.

Importantly, and contrary to what some have suggested about our efforts, we must ensure appropriate investor protections for our long-term Main Street investors in any action we take. Here I note that our public capital markets protect our Main Street investors in many ways including that our long-term Main Street investors get essentially the same terms, they get the

same deal as our long-term institutional investors. We should think about replicating that in the private capital markets.

Let me pause and deviate a second from my prepared remarks. If you look at well-managed pension funds across the spectrum, some have no private equity, some have a lot, but on average they have a fair amount of private equity exposure for their long-term constituents. It seems odd that when you're investing for the long term as an individual in your retirement account that you would have no such exposure when the professionals all think that kind of exposure in today's marketplace makes sense. That asymmetry, dichotomy, is something that we should at least look at and recognize.

Okay, next. Second, as you well know, small and medium-sized companies are increasingly relying on our private capital markets to raise capital. We have found that these markets are all too often not functioning so well between the very early stage and, I would say, almost medium-sized stage. You guys have identified this well, from two, three million dollar valuation to a fifty million dollar valuation, the road, particularly the capital raising road, is very bumpy, very cumbersome, and takes a long time. For innovative companies, that time means the market can change and

their opportunities can fade, or competition from others, maybe larger companies, 00:10:24) anyway, limit their opportunity set. I really want to hear from you on how we can bridge this gap, make it easier for those companies to access capital while maintaining investor protection.

Again, I'm going to deviate from my prepared remarks and say that for the past two weeks I've been traveling, meeting with central bankers and regulators around the world, the nimble nature of our small- and medium-sized businesses, our capital and labor markets, remains the envy of the world; it enables us to adjust to changes in the economy, changes in technology. We need to do whatever we can to continue to facilitate that. It is a comparative advantage for our country and it's one that we should continue to recognize. So your work is very important to us.

And I think our speaker is not yet here. Or is here? Okay, I was going to fill the time and say ask me any questions you want until -- but you have spared me from the press conference-like grilling, so there you go. I'll come back and answer any questions you want sometime in the future. Thank you.

MS. GARRETT: Thank you, Chairman Clayton. Before diving into specific areas of the Harmonization

Release, we thought it made sense to step back to look at the bigger picture of how small companies obtain capital, which is much broader than just through the securities laws. To help give context to the various situations in which securities laws may come into play, it seems relevant to have the fundamental data on how entrepreneurs finance new businesses, whether it be bootstrapping, credit cards, family or personal savings, bank loans, friends and family, or venture capital.

Our first guest speaker is Ross Baird. Ross has an interesting biography. He founded Village Capital, an active venture capital firm that invests in so-called overlooked entrepreneurs. Ross is also the CEO of Blueprint Local, a platform to help people across the country to invest in their own communities. And the committee has extended an invitation to Ross for this meeting because he also wears the hat of innovator and residence at the Kauffman Foundation. Ross has authored multiple reports for the Ewing Marion Kauffman Foundation on the state of access to capital for entrepreneurs. The Kauffman Foundation supports a number of programs including many that offer guidance, resources, education, and events for aspiring and existing entrepreneurs. They have published multiple reports with fascinating data, and we look forward to

hearing about those findings from Ross.

Welcome.

MR. BAIRD: Great. Thanks for the invitation, and Chairman Clayton, thanks for inviting me. Sorry to not give you open mic time, but hopefully we make this worth everyone's while. It's good to see a lot of familiar faces, good to see a lot of new faces. I really, really appreciate the introduction. I'm hopeful to give you a couple of insights that will lead your discussion.

I come at this from two levels. At the one-foot level as a founder of a series of different funds over the last 10 years investing in entrepreneurs and small businesses in the distressed parts of the country. I've had the privilege of coming across a lot of you in that work. And second, from a 100,000 foot level with the Kauffman Foundation, which has been the leading backer of entrepreneurs and entrepreneurial initiatives in the country. And I want to talk about some of the research we've done on the latter of what is happening in the country as entrepreneurs try to access capital, and just a few observations that may be helpful for this committee to consider as you do really important work.

So I, about two years ago, worked with Kauffman Foundation to do a study of -- there's a lot of

conversations whether it's venture capital or lending, it's very obvious that for a lot of businesses and a lot of investors, the market is not working particularly well. We looked at the data and it turns out there's a lot of focus on getting venture capital to more places, a lot of focus on getting small business loans to more places, and it turns out 83 percent of businesses that start don't access formal forms of capital. Fewer than 1 percent of businesses access venture capital; about 18 percent of businesses will get a loan. But 4 out of 5 businesses don't access any form of capital. For many of them it's they don't want it or they're not investable, but many more face structural barriers that this committee's looking at.

As we look a bit deeper, this is from census data, here is how entrepreneurs and small businesses finance their start-up or their growth, the other 83 percent, so to speak. Here's a breakdown. You see businesses starting with personal savings, personal credit cards, bootstrapping, no outside capital, home equity loans.

One of the things that the data shows us is despite a boom in the media on entrepreneur activity, entrepreneur activity in the U.S. is hovering at near a 40-year low. And one of the things that we saw in 2008

was the great recession for the bottom two-thirds of families wiped out savings, home equity, a lot of the sources of capital for small businesses. So without rethinking how capital flows to businesses, it used to be a lot of businesses would bootstrap their start-up. You know, 2 out of 3 families don't have boots, so to speak, post-recession and it creates real geographic, real demographic, real gender barriers, real race barriers that are really important to dig deeper into.

Just to tell a story of a business that is a meaningful business, creating meaningful jobs in the country that doesn't fit the venture capital profile, doesn't fit the small business lending profile, a firm I founded, Village Capital, in 2012, one of our first investments was this company called Fin Gourmet. They're in Paducah, Kentucky, southwest Kentucky. Unemployment in the county was about upwards of 20 percent in 2012.

And this woman, Lula Luu, she's an immigrant from Vietnam who settled in the Mississippi Delta and realized two things: one, Asian carp is a huge environmental threat; and two, people love to go fishing. And so she developed a brand around Asian carp, which was not selling well in the mainstream market. She rebranded Asian carp "Kentucky Blue

Snapper." It's like how Chilean Sea Bass is actually a muckraking bottom-feeder.

And she would literally give unemployed people in Kentucky fishing rods and go out and they'd catch the fish, rebrand it Kentucky Blue Snapper and sell it. Now, you can buy Kentucky Blue Snapper in high-end restaurants in New York and San Francisco.

And so we met her. She was doing about $250,000 a year in revenue. She was about two years old. She was employing 12 people. She needed $250,000 in growth investment. No bank would touch her because she was two years old and venture capital said, well, that's not really what we do.

So we did a kind of alternative investment structure where we did -- we (18:22) a group of investors; we put in $250,000; about half the money was local, half the money was national from funds like ours; and we did a revenue royalty share where we said we'll get 5 percent of your topline revenue until we get a three times repayment, you know, or 10 years passes, whichever comes first.

So with that $250,000 she built a processing facility. Today she's doing about three million in revenue. She's employing 50 people. She's in a county where she's one of their largest most meaningful

employers.

I bring this story up because it's very easy to get in the policy weeds, but this is what the 83 percent look like. And it was just a couple of people at an individual level in one town in Kentucky that made this investment happen. But what the Chairman is talking about, institutionalizing this kind of long-term equity investment in companies like Fin Gourmet, will make a massive difference in our business environment.

So why aren't more businesses like Lula's getting financing? We looked at a few barriers in the Kauffman Research. Number one, and the Chairman talked about this a bit, there's a real gap between institutional asset management and the needs of everyday businesses in America. So we interviewed over 300 institutional investors, pension funds, endowments, et cetera, who manage more than 1 billion. Fewer than 5 percent said they would even consider an investment fund of less than 100,000 million just because of sizing and time, and it takes a lot of time to do diligence on a fund manager.

So the way the regulatory framework should look at this is the way the market sits today. It is massively privileging large funds that are doing billion dollar funding rounds in large cities. And so if you

are a fast-growing tech company in San Francisco, the institutional framework kind of pulls capital towards you. If you're a business that needs $250,000 of growth capital in southwest Kentucky, there's just not plumbing to get capital to what you're doing.

I think the second issue -- so that's kind of a demand side issue. Businesses are not big enough to access institutional capital. And then there's a supply issue which I know, for example, Youngro and NextSeed in Houston has been extremely focused on. The average person -- you know, our pension might be invested in a venture capital fund that's invested in growing companies, but you can't invest in it. And this is exactly what you were saying to kick off the day.

So if you look at, for example, I was in Baltimore yesterday and there's a group of young professionals, young African-American professionals, you know, these are doctors and lawyers, people making, you know, six figures, like reasonably great salaries for Baltimore, and they want to invest in growing businesses in Baltimore, but even making, you know, $100,000 a year as a lawyer in Baltimore you don't clear the accredited investor bar, let alone the qualified purchaser bar. So you have young, black professionals in Baltimore wanting to invest in black businesses in Baltimore and there's

just no institutional way to do it.

So, you know, and if a very wealthy person, you know, if you make over $100,000 you're one of the wealthiest people in America. If that person can't invest, what happens with the vast majority of the country? So there's a lot more we can go into, but there's a barrier on companies not being large enough to receive capital, and there's a barrier of investors not being wealthy enough to invest capital.

And then I think the third barrier is structural. I tell the story of Fin Gourmet, and this is where Kauffman's work has really focused over the last year. So venture capital is incredibly important and fewer than 1 percent of businesses raise it. Small business lending is incredibly important, only about 1 in 5 businesses get a small business loan. The average business is like Fin Gourmet in that they would be seen to be too risky for debt and not unicorn-y enough for venture capital. It's very unlikely that Fin Gourmet will be a billion-dollar business but that doesn't mean they're not an important part of the country's economic fabric.

And so there are a number of different models that we've looked at that are more similar than different. The revenue share model that I talked about with Fin Gourmet; there are profit sharing models; employee ownership models; pay for success. There's a model called performance-based equity where I invest equity in your company and when you hit certain revenue triggers you pay investors a dividend. They're all somewhere on the spectrum in between equity and debt, and our hypothesis is these models fit a certain type of company. I don't think it's the whole 83 percent, but it's probably 15 or 20 percent of businesses that are investable, would provide a good return on investment to investors, create meaningful jobs, but for whatever reason don't fit the current regulatory framework which is highly focused on what a (00:22:57) bank should be regulated, how a venture capital fund should be regulated. So that's just an area for discussion and exploration.

Kauffman actually launched a pilot called the Capital Access Lab where Kauffman as a foundation would take LP positions in funds that have some of this profile between equity and debt. There were over a hundred funds that applied from 32 states. 55 percent of these funds are women-run; 42 percent are led by people of color. As we look at alternative models that are a bit more grassroots, we see very different managers, very different entrepreneurs than the stats

you see on venture capital. So that is hopefully what you guys were looking for. That's an overview of what we're seeing.

I'm happy to go deeper, I just hit a bunch of bullets and I'm -- I don't know how much time we have but I'm happy to go deeper if you'd like on any of those topics or whatever is of interest.

Yes.

MS. MOTT: Ross, thank you so much for this presentation, and this data supports what a lot of what I see. So one of the things I do run into in the region I'm in, which is mid-America, is that there are revenue share funds which they are starting to, you know, they're starting to grow. The bar seems to be a million in revenue before they'll get a revenue share investment, which sometimes by then you're bankable, you know what I mean?

MR. BAIRD: Right, right.

MS. MOTT: So they're still in my, you know, just my thoughts about what I'm seeing, not that I have any data points, but what I'm seeing in the marketplace is that there are revenue -- there's that gap between what the Fin company in Kentucky, so probably they would fall into that gap because they're not making that million dollars. So just something to say what I'm

seeing in the marketplace.

MR. BAIRD: Yes, so I would say it's easy to say this is, you know, this is the landscape; what's the answer. And if you jump to, for example, a revenue share fund, there are, for example, there's a company called Lighter Capital that has a hundred million under management. They're more -- their risk profile is much more kind of mezzanine debt than early stage equity. It would be extremely unlikely that Fin Gourmet could get an investment from Lighter Capital, and that's fine. I mean there are other models that are looking at financing of earlier stage businesses that look more off of dividends based off of free cash flow or look at profit sharing versus revenue sharing when companies reach profitability.

One of the things that we looked at in this study is we looked at a lot of the early private equity funds and we talked to people that were early on at funds like KKR and Bain Capital and Wesray out of New York. And they said, you know, we were all doing very different things; it was just kind of people trying to figure out how to finance private companies, but we spent a lot of time in working together around concepts and categories and the creation of an asset class, because of even though, you know, Wesray and Bain

Capital in 1981 were competitors for limited partners, if investors make an allocation to private equity as a category, it's actually better for both funds.

And so one of the things that I am seeing is these funds that are trying to solve for in between venture capital and debt, some of them don't solve Lula's problem; others do. We are seeing these funds viewing themselves as more similar than different, saying here's the category that we're going to.

So I would say what you're seeing in the market is right and true, and then there are other funds that are probably more solving the gap that you care about. And we should, as we look at it from 100,000 foot level, is you think about the work you're doing (00:26:54) think of, you know, what Youngro is trying to do in Houston which is get people in Houston to finance Main Street businesses in Houston, as a category is probably more similar than different than how a business in Paducah that can't access venture capital gets financed. And if you think about it as a category in a regulatory framework, I think it would be really useful.

MS. GARRETT: I have a question. What stage do you believe a company needs to be at in order to get the institutional investments and so therefore, you know, just thinking about how many companies are not at that stage yet and so the population of companies.

MR. BAIRD: Yes, I think there are two things to unpack in that question. I think, I mean the biggest risk of just anybody can invest in any company is it opens things up to massive fraud risk, and that's what a regulator should be very worried about. I would say that there is a -- I mean I would say there's a certain stage of maturity where companies have had for a year, two years, I'd say there -- I'd say the earliest solvable gap is where companies have two or three years year-on-year revenue growth, fulltime employees, they are going concerns. That is one category that I would say is incredibly difficult to finance if the company doesn't have or invent a hockey stick growth trajectory that gets venture capitalists theoretically interested.

But so I'd say the easiest place to start, knowing that there are tens of thousands of business that should get capital and don't, is businesses that are profitable or close to it and reliably growing and do not fit banks' current underwriting algorithms and do not fit venture capitals growth trajectory. And I would say we try to figure out of the 83 percent, what percent. It's probably 8 to 10 percent of businesses that are reliably profitable and growing and haven't -- just don't fit into institutional categories.

The second thing is if I own three restaurants in Houston and I want to open a fourth, a generation ago a community bank would have looked at my reputation and extended a loan saying these three restaurants are doing -- today, banks would say, well, it's a start-up restaurant, those are incredibly risky, why would we do this. So I think, you know, proven independent businesses that are trying to grow or move into new categories where, in an age of much more diversified banking reputation and track record, would have mattered more, but -- and I think this is the world that you're very much in with NextSeed.

So I'd say that's a second category of kind of small businesses that want to grow but don't fit. I'd say that's probably another 5 to 10 percent. Those are the two places I would start to look at what could be better addressed.

MR. LEVEY: Hey Ross?

MR. BAIRD: Yes.

MR. LEVEY: Thanks for coming in again. Do you get a sense that sort of the trends are getting worse here --

MR. BAIRD: I do.

MR. LEVEY: -- that, you know, as opposed to stabilizing or even improving a little from sort of when

you did your study?

MR. BAIRD: I think the trends are getting worse for two reasons. I think, one, on the capital side, and I think both of them are concentration issues. So on the capital side, funds have every incentive to be as large as possible. Why would you raise a two-billion-dollar fund if you can raise four-billion-dollar fund. And so one of the issues is you have fewer and fewer managers out there who are taking -- like if I'm a first-time manager, I will take some risk to invest in a business that no one else is investing in because I want to prove my track record, I want to make my career. Larger and more consolidated funds mean fewer and fewer decisionmakers. I mean 2 percent of venture capital goes to women; less than 1 percent goes to African-Americans and Latinos. 2 percent of decision-making partners at venture capital and private equity firms are also women; same stats with African-Americans and Latinos.

So I think we have a concentration of decision-making power over capital on the supply side that is hugely problematic. And it just means more and more things like the SoftBank vision fund and fewer 50- to 100-million dollar regional funds that take local risks.

And then I think on the demand side, you have -- you know, when I started Village Capital in 2009, Facebook had just gone IPO, and a question gets asked all the time today which wasn't even asked 10 years ago, which is oh, you're doing something online journalism or whatever. Facebook owns that category, you can't possibly compete, dot, dot, dot, therefore you're not investable. It's seen, I think today, much more difficult for businesses to compete with Facebook, Google, et cetera than it was 10 years ago. So they're huge competition issues on the small business and start-up side. So I do think it's getting worse, unfortunately, because just because of bigness.

MR. LEE: Ross, thank you for all the work you do. I know, I mean you're one of the, literally, experts on this through Village Capital and BluePrint that you're really focused on small businesses.

So one of the questions that we go through, and I'm sure you do as well, is when you're now presenting these opportunities in these local businesses as you're being very clear, right? These are not unicorns, but they're solid businesses and there's potential.

One of the common feedback from investor advocacy groups and interest, sort of interested personnel rather, they're well-meaning, right, but they're very conservative investors and they're basically saying that's high risk, right? Restaurants go out of business all the time; retail investors should not invest in such businesses as a blanket category.

How do you address those points and how do you respond to that? Because I think that's the biggest barrier to, at least in my personal opinion, these issues that we have today because you've basically established institutional capital as a systematic matter is just not going to invest in these businesses, right?

So we're now thinking about, okay, so who is the category people who are willing to invest, and the natural answer is basically retail investors. So how do you adjust that dynamics in a professional way for the investor protection kind of considerations?

MR. BAIRD: I think this goes back to my earlier comment of how important it is to create categories or asset classes. So, for example, the Kauffman Foundation, 20 years I think how Kauffman -- what Kauffman views success in this exploration, and this goes back to Carla's question as well, is 20 years ago angel investing was not a term. There were a bunch of rich people around the country who did individual checks into individual deals, and Kauffman Foundation

said there's a lot of stuff going on around the country that's more similar than different, and actually it could be really good for entrepreneurs if this becomes much more common. So Kauffman founded and funded the Angel Capital Association; they gave grant funding to a lot of early angel groups.

Today if I say I am an angel investor, and you're in the entrepreneur world, you generally know what that means. But the intentional creation of a category really, really accelerated that. So I think there is a type of Main Street business, for instance, that is riskier but higher return than debt, lower return but more liquid than equity; it's probably more similar than different. And if you said this is the category or asset class that we are investing in, you know, revenue-based businesses or whatever, I'm not a branding whiz, but people are, how do we invest in that category.

So if you said today -- and real estate has done this incredibly well -- if you said, I like investing in multifamily housing, people know what that is versus commercial real estate versus single-family housing. They all have different risk and return profiles. I don't think we have that level of granularity around different types of business investing

and so, you know, one thing in your committee, like, how do we create and think about and regulate and model different categories because if there were an equivalent, you know, if restaurants and, you know, growing retail and all that are a category 10 years from now, and say I'd like for you to make an investment in these type, this category in Houston, people would understand kind of what that mean. That may not be the right answer but that's how I've been thinking about it.

MS. HANKS: Thanks, Ross. I think (00:35:51) is being too modest and he doesn't want to raise this, but so many of those 83-plus percent companies would be ideal for crowdfunding and (00:35:59) for a platform like Youngro's. Do they know that this is a thing? And is there any way we can reach out so that they know that's a resource for financing?

MR. BAIRD: I would say the vast majority of businesses when I've talked to about crowdfunding say it's just too complicated, why bother. It seems great but it seems like it's incredibly complicated. I mean intermediaries like NextSeed that make crowdfunding incredibly easy for small businesses are very important. So that's kind of one. I think the intermediary framework of crowdfunding is not -- I mean I think it is in the top half of the first inning of what it could be,

and that's really important.

I think the second piece is investor education. I think that the average -- I mean one thing that kind of annoys me is there's a huge paternalism sometimes talking towards investors saying, oh, the average person doesn't understand how they can make money off of an equity investment in a company, dot, dot, dot, therefore they shouldn't. The average person who has a mortgage, even if they don't have a college degree, knows that owning a home can build wealth. Like people understand ownership but I think there has been a tremendous amount of focus in our economy and as homeownership is a way you build wealth, business ownership is not -- there's not the same level of fluency.

So think just basic, like, here is how you make money owning your business: either if you work for a business the employee ownership -- I mean people even in companies that we have invested in that have goals of their eventual exit being an ESOP or -- they have a very difficult time explaining to their employees, here is why you should take a lower salary in exchange for equity, in a lot of cases. And so I think there is a -- if we're going to create community wealth, I think ownership creates wealth a lot faster than income does.

And there was a lot of studies around this. And so ownership as north star is just a really important concept that is very poorly socialized, outside of home ownership.

MR. TORBERT: Ross, good to see you again.

MR. BAIRD: Yeah, great to see you again.

MR. TORBERT: I want to ask you a quick question about the sector buys that occurs because many instances some of the (00:38:33) focused on tech and so on. Can you speak to some of the other sectors that you can find in other areas like the Midwest or the Gulf where I'm based that are actually -- that do offer high returns and potential for investment. Manufacturing. There's a high density of other strong sectors that exist that are investable but no one seems to focus on them, and why should they.

MR. BAIRD: Yeah, I mean I do think that there is a geographic bias of understanding -- investing in what you know and understand. If you look at what SoftNet or (00:39:05) has done investing 150 million in the middle of the country, the investments in the Mississippi Delta region, you know, from St. Louis up to Chicago down to Louisiana are much more ag tech, manufacturing, logistics, and they should be; those are strengths of the heartland, they tend to be much more

consumer-focused in L.A. or, you know, and gov tech in D.C. And I do think that there is a somewhat institutional bias that VC investments should be high-growth consumer tech investments.

But when you have funds that have different regional winzes, they tend to have very different portfolios, and I mean one of the things that Kauffman research shows is smaller funds actually outperform larger funds. And I think this goes back to the point that we were talking about, smaller managers are more motivated to invest in different businesses which tend to be outliers. But smaller funds also have, I've found, much more sector diversity than larger funds.

MR. TORBERT: Could you speak to the time period that you used for that, whether it's 10-year, 20-year, et cetera?

MR. BAIRD: Ten year.

MR. TORBERT: Yes.

MR. BAIRD: Some of the most interesting funds I see in the country tend to smaller, tend to be hyper sector -- I mean there's a fund here in D.C. called Anzu Partners that basically goes to labs, university towns, like third and fourth -- I mean cities that are like 18,000. They find the one inventor with the one technology that it's never come across even with capital

and they invest in it and license it, and they've done remarkable well with, you know, lasers coming out of national labs that VC wasn't looking at. I mean Rise of the Rest Fund, this is your exact thesis. So I do think this kind of answers your question. There's a kind of homogeneity of large venture funds where competing over getting in the same four or five deals is just -- it's not really a free market versus finding the opportunities that other people aren't.

MR. TORBERT: Would you argue that that distorts the market --

MR. BAIRD: I think completely.

MR. TORBERT: -- valuation --

MR. BAIRD: Completely, completely. I would say businesses that are consumer tech on the coast as a category are overvalued, and if the SEC is listening this is not investment advice or anything -- you guys are lawyers, whatever disclaimer --

MS. MILLER: You missed the earlier disclaimer, on behalf of everyone you're covered.

MR. BAIRD: Okay, great, all right. So all disclaimers aside, I'd say they're overvalued because, and if you follow the money because institution LPs are incentivized to invest in large coastal funds for various structural reasons we went into, which have a

very specific profile so these, you know, these funds compete over a relatively small number of businesses.

If I've got a very compelling, I don't know, in San Antonio if I have a very compelling drone technology in San Antonio, there aren't a lot of funds that are looking in San Antonio. There aren't a lot of funds that understand drone technology. It's systematically undervalued I would say. And I think that's systemic risk.

I mean if I were a regulator this is how I'd be thinking about it. And, you know, SoftBank is doing a great job proving this point. VC funds say we are diversified and that mitigates risk for institutional investors. But if you're diversified in a monocrop culture of companies that are all following the same playbook and you realize that all of these companies are heavily incentivized, for example, to bias growth over profitability, if you hold a diversified portfolio of extremely risky assets, diversification doesn't matter.

So I actually do think we have systemic risk in the VC world among mainstream funds because of these various structural issues that we talked about.

MR. SEATS: And also one interesting side effect, you get large enough and the largest asset managers have more lawyers than the SEC and so try to think about an arms race of regulation to change the dynamic is challenged from the start.

So Ross, I totally agree with your world view, I think it's a super logical framing. And also you dropped in a little bit of a history lesson on origins of private equity and origins of, sort of, angel investing as a category.

So one question I have, both of those stories have a similar thread in that the construction of the new category, the new asset class, happened in the private market. It didn't start from a regulatory framework and get pushed down. So think if we could all agree that, you mapped out hey there's a big opportunity here and maybe there's something in between debt and equity, this is different, and we're missing a nomenclature in a way that sort of categorizes this, I guess the question I'd have for you is how do you think about the work of this group and the Commission in terms of being able to influence how the private market creates those categories with the way that they invest and the way that they think about approaching fund construction and whatever else.

MR. BAIRD: Yeah, I mean I would say something around, you know, what can you, the SEC as a regulator do is a very powerful and limited toolkit. So things

like the venture capital exemption. The cap of the -- I believe it's a hundred million, is that right? I'm turning to my lawyer friend, (00:44:30). So the venture capital exemption is capped at a hundred million. If you were to say -- so running the numbers, let's say you and I are, you know, well-educated white guys and we're partners at wherever, Mackenzie, and we have some idea, we go and raise $100 million, we get 2 percent, you know, that's 2 million. We're making a million at Mackenzie. We see this all the time, say, well, we should pay ourselves what we were making at Mackenzie, we make a million dollars each, that means we have, you know, maybe a little bit of money for analysts or whatever, but there's very little -- there's very little opportunity for growth in regional or demographic diversity because venture capital funds are small and pretty top-heavy.

And if you were to say if you are a fund that, I don't know -- I mean and there are other regulatory frameworks from SBA or the Office of the Comptroller of Currency (00:45:24) Reinvestment Act and qualified small business credit. If you said, you are a venture capital fund that invests more than 50 percent in low and moderate income (00:45:33) tracks or in X, Y, Z excluded populations, you know, women, people of color, et

cetera, your venture capital exemption is now 400 million. I'm just making this up. Something to encourage the stimulation of smaller funds using SEC exemption rules or more regional funds or more economically distressed areas, it's just -- that would be a line of -- I'm already out planning my coverage, I don't know any more than I've just said, but something to encourage smaller funds that go to undercapitalized places is something to think about.

I think the second thing I would think about is probably part within the SEC's purview and part outside, and it's how these funds are regulated and taxed. So for instance, one of the issues with revenue-based investing is it's if you structure it like equity, you make it as capital gains, but it's incredibly complicated from a regulatory side if you structure it like debt, it's simple from a regulatory side but it's taxed like ordinary income.

So people want to go with the incredibly -- so if you say something around employee ownership or alternative investment structures have a much simpler regulatory framework so that people pursue it in a tax-advantaged way, that would be another thing I would look at. So just general regulations around fund construction I would say.

And then the third that is who's an accredited investor, who's a qualified purchaser, are there ways -- because a lot of these things, I mean the venture capital exemption I don't believe has changed since the '40s. It was set at a hundred million in the '40s. I might be -- it was certainly -- it has not kept up with inflation. So these are -- I know I'm just throwing out a bunch of bullets for you guys to chase down and it's easy for me to opine and you to do the work, but these are systematic things we've observed that you could actually work on.

MS. MOTT: So Ross, I'm sitting here thinking, as former chairman of the board of the Angel Capital Association, I'm thinking about investor behavior so people feel comfortable investing in what they know and understand. Then I'm tying that into I went back to my hometown that I grew up in, it's in northwestern Pennsylvania, small town of about 11,000. Now at 5,000 because of the decline of manufacturing. And one of the major companies in that town was Werner Ladder company. It moved to Mexico and all the jobs went there as well.

And what was interesting to me was tied to what you were talking about in sectors and people invest in what they know, a group of people got together, accredited investors of course, that know manufacturing,

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got together and put together a framework for a small, that can use that Werner Ladder facility and make it into specialty aluminum extrusion company, maybe saved 50 jobs or something like that.

So around that thought, if you think about people investing in what they know, would pulled investments with people with expertise in those areas, like you were talking about with real estate, would it make sense to have them, because they know manufacturing, right, be managers. And what we see is those who get involved with companies because they know that industry, help that company, mentor them, make introductions, they tend to be more successful. So along that line, you know, getting professional managers maybe manage that know those industries, right, would probably serve that best.

MR. BAIRD: I think this goes to the question of small -- making it possible for smaller investors and smaller funds. It's just that a very large thing for all of you to work. So I completely agree with you. We were working in Austin, Texas earlier this year on a – there are two census tracks in Austin that were historically labeled by the city "The Negro District". That's literally what it was called, on signs and things, in 1928. A hundred years later, there are no

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health clinics, there are no grocery stores. So there was this — and there are these retired doctors in Austin who are very familiar with public health challenges. And there was this project where they were trying to get people interested in how to get invested in this community health and wellness effort, and have a health clinic, grocery stores. Very -- very Next Seed-y. It's a cool idea.

So there is one guy, a very wealthy guy, a qualified purchaser, very. And he was a retired doctor. He wanted to lead the investment. And we talked to him and he said well, you know, go talk to my wealth advisor in New York City. And I happened to be in New York the next week. And it's like, the guy lives five minutes from the -- and it's like, you have to fly to New York to ask permission to send $500,000 five minutes east. And the guy said, that's idiotic, that's too risky. Why would he ever do that? Even though it's something that he knew and understood. And so the layers of kind of -- I mean, this guy is worth enough to where losing $500,000 would not impact his lifestyle and he wanted to do it.

And I don't -- I don't -- just the layers of complexity and how money flows in the economy prevents a lot of things like that from happening. And whether or

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not -- I mean, the Austin thing ended up happening, but there's a -- there's systematic thing. So I think what you're saying is exactly right, and there are layers of regulatory complexity that prevent that story from happening more often.

A PARTICIPANT: -- purchasers, there's been sort of a mix. And maybe you sort that money a little to see where you're investing it. Is that something that you would consider?

MR. BAIRD: I will tell you a problem that I would love for you to think through solving. Because right now, I don't have a great answer. And it's the story I told earlier about the, you know, young African American professionals in Baltimore who on average have a net worth of about $250,000, who want to invest in real estate and growing businesses in very poor parts of Baltimore. So you know, we at Village Capital and with partners like Rise of the Rest have invested all across the country. We've gone deeper into a few ecosystems where we've been particularly active. Baltimore is one of them.

MR. FOX: Ross, I'm sitting here thinking about this, and I guess I have a couple different thoughts. One, I keep hearing about this, approaching it from hey, we need more individual investors in the

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marketplace. And I kind of wondered about that because I'm kind of thinking well, gee, if we get more individual investors in the marketplace, well, isn't that just going to -- isn't BlackRock or one of these other big -- you know, how are we going to end up having more individual investors invest in these big uber funds, right?

MR. BAIRD: Mm-hmm.

MR. FOX: I'm not sure that that's going to ultimately translate into individual investors in FIN, you know, in Kentucky, you know --

MR. BAIRD: So, if Andreesen Horowitz and BlackRock form a partnership to say --

MR. FOX: Right. Yeah, yeah.

MR. BAIRD: -- you, schoolteacher in Joplin, Missouri, can --

MR. FOX: Right.

MR. BAIRD: -- now invest in Andreesen --

MR. FOX: Yeah.

MR. BAIRD: -- I don't think that solves the problem --

MR. FOX: Right, exactly.

MR. BAIRD: -- that we care about solving for policy.

MR. FOX: But it goes back to -- I'm trying to think through, okay, how do we get to solving maybe the question you very articulately posed? How does the Vietnamese, you know, lady in Paducah, Kentucky, get funding? And you know, okay, she needed a $250,000 investment. And you said, you know, very articulately, the way it is right now is it's easier to do a four billion dollar fund than a two billion dollar fund. Well, frankly, even a two billion dollar fund isn't going to be interested in making a $250 million (sic) investment.

MR. BAIRD: Never, yeah.

MR. FOX: It's too big -- I mean, too small.

MR. BAIRD: Mm-hmm.

MR. FOX: You know, even on a $250 million (sic) investment in Paducah, Kentucky, what I'm thinking is gee, the deal cost alone had to eat up a lot of your investment cost, right?

MR. BAIRD: Mm-hmm.

MR. FOX: And I'm just wondering, as I'm thinking it through the role of this committee and the role of this SEC, are there some things around the role of technology and regulation that could be reducing the role of deal costs?

MR. BAIRD: Completely.

MR. FOX: Right? If I think through, are

there ways that technology and other things could be going on? Could there be kind of standard agreements? Could there be standard ways of introducing investors through technology and other things, right? We're getting -- I don't want to -- I know there's a lot of attorneys at the table. But getting some of the attorneys out of the process. Getting things like that to where you could do a $250,000 investment with little cost, or you know, reduce costs to where you're not having to spend $50,000 or more to do a $250,000 investment to where the hurdles, the investment hurdles just aren't so high to overcome.

MR. BAIRD: Mm-hmm. Mm-hmm.

MR. FOX: Because it seems to me that that might be one of the biggest barriers, right, to prevent a lot of that. And I'm wondering if what isn't maybe a lot of the barrier to a lot of these things -- and maybe I'm completely wrong -- isn't just that gee, it's just so hard to overcome the transactional costs to do a $500,000 investment even though it's a decent deal in a non-traditional bankable you know, deal for a $500,000, $750,000 investment, it's just not worth it.

MR. BAIRD: Mm-hmm.

MR. FOX: And I'm wondering if there's some things to be thinking about, using you know,

modernization technology and other forms of regulation to reduce that. To reduce those barriers. And advancing that so we can actually then bring more capital to those transactions.

MR. BAIRD: Yeah. I mean, one thing that Kauffman thinks a lot about is some -- did I over -- something like a FICO score for small businesses. So this is something that has happened -- if you look at how the FICO score evolved historically. A lot of banks have their own propriety algorithm and you know, in the '50s and '60s, and there was clear regulatory guidance and there was some kind of public engagement. But it was generally seen to be a good thing if there were a way to compare credit. And there are all kinds of FINTEC companies out that say the FICO score is problematic and we have ways to improve on it, and that's all justified. But getting, having a FICO score that was generally agreed upon by lenders played a major role in expanding home ownership in the U.S. as a positive outcome that seems like the kind of thing this committee would want to talk about.

So if we were to say something like here is Fin Gourmet in Paducah, and their business FICO score equivalent is 760 out of 800 and these are the five ways that everyone looks at it, that would cut some element

of the transaction costs quite a bit.

MR. FOX: Well, but also there's a standard mortgage contract and you know, typical closing attorney costs are a couple hundred bucks now --

MR. BAIRD: Right.

MR. FOX: -- or a thousand dollars, right, and it's not a customized contract anymore, and that sort of thing too. Right? I think there's a number of different things that go along with home ownership in addition to the FICO score as well, right? And I'm just trying to think through, I think there's a lot of different things, right? If I think through all of the probably things you did as you made your investment, right?

MR. BAIRD: Yeah. I mean, it was, it was insane.

MR. FOX: Yeah. It was insanely complicated, right? And I'm just not sure -- I mean, my guess is if you had the passion for making that investment, it's probably not replicable.

MR. BAIRD: Right. And we had a -- you know, we had an attorney who happened to have grown up in Paducah, and he did an insane amount of pro bono work just because he personally loved this story, and that's not a replicable story. But I think that what you're saying about standard mortgage contracts -- I mean, in the '60s the U.S. -- I mean, the policy -- this is more of a values question than a technocratic question, but in the '60s the U.S. said home ownership is a national goal. We are going to do a number of things at the SEC and at HUD to make home ownership easier. And whether or not that is a valid policy goal is a policy question.

MR. FOX: Right.

MR. BAIRD: But if you say our goal is to remove barriers in access to capital for small businesses across the government, that is a policy goal. And if you do that, you're right, there are 20 different things that could reduce the transaction costs from five figures to hopefully three that are steps I think this committee would, I think, be well-served to spend some time talking about.

MR. FOX: Okay. Because again, I just think that if we're thinking through this, I just don't know. If we don't contemplate that as well -- I think we can talk about all these other issues, but if we're talking about hey, how do we get these small businesses -- you know, we're never going to address how do you really, realistically get to -- and maybe it's crowdfunding and how do we get to make that easier and other things. But yeah, that's a technology play that maybe again, reduces

the cost of capital again. But it just seems to me that if we don't address some of these other things, we're never, these smaller deals are never going to happen because they're just going to be too expensive because of the transactional costs in them, so.

MS. GARRETT: I also wanted to ask or think about --

MS. PATODIA: Hey, guys, this is --

MS. GARRETT: Go ahead, on the phone?

MS. PATODIA: Hey, guys, this is Poorvi.

MR. SEATS: I had a quick question. Sorry.

MS. GARRETT: Go ahead.

MR. SEATS: All right. Real quick. Can you just tell me where your capital comes from?

MR. BAIRD: In the funds that I've started, it's primarily qualified purchasers so, and institutions, so the aims of what I've done in my career are democratic. The sources of capital are not. So I am I think living the exact issue for a lot of things that we're talking about, that we're talking about here. So a lot of, a lot of my observations are definitely borne from experience of what we're trying to do with money we've raised and the restrictions around the type of money we can raise.

MR. SEATS: Well, let me ask you a question.

If you -- if the money -- if you -- if there were, if we were to create a regulatory regime or recommend a regulatory regime that would enable you to access capital from non-accredited investors with the safe harbor or maybe in conjunction with a certain amount of qualified purchasers, in sort of a mix -- and maybe you sort of set money a little to see where you're investing it. Is that something you would consider?

MR. BAIRD: I will tell you a problem that I would love for you to think through solving, because right now I don't have a great answer. And it's the story I told earlier about the, you know, young African American professionals in Baltimore who, on average, have a net worth of about $250,000, who want to invest in real estate and growing businesses in very poor parts of Baltimore. So you know, we at Village Capital and with partners like Rise of the Rest have invested all across the country. We've gone deeper into a few ecosystems where we've been particularly active. Baltimore is one of them.

Baltimore's racial history, history of institutional racism, redlining, et cetera, has left a very unequal city. And it is right now kind of a noblesse oblige, almost a philanthropic mindset where wealthy white people in Baltimore will from time to time

give a little bit of grant funding to entrepreneur incubator programs. But not put real money in. But if you talk to young African American professionals in Baltimore, they would like to invest real money in, like, their actual nest egg into the black neighborhoods of their city, A, because they think as a financial decision they're very undervalued. B, they're very kind of personally motivated. So I talked with a group of them yesterday. They're neither credited investors nor qualified purchasers. But I mean, they're securities lawyers. They're highly sophisticated investors. And currently there is no way to make money flow.

So I use that as kind of a focusing anecdote. You know, getting the shopkeeper in Baltimore to invest $25 into a $20 million Baltimore fund is probably the next step. And that's actually you know, the current step for NextSeed and others. But I think for me, like, getting, you know, upper middle class, you know, whether it's -- whether its Baltimore or Kansas, getting upper class people from places that are not well-capitalized, that are not accredited investors or qualified purchasers to invest in the business growth of their own city or community is -- I think there is appetite for that today all across the country, and the regulatory framework makes it extremely difficult today.

A PARTICIPANT: And let me -- let me ask this question. Not to throw more regulation on you, or any regulation on you for that matter. But if you -- if you had to -- sort of maintain certain licensure that qualifies you to take money from non-accredited investors, would you do it?

MR. BAIRD: I mean, I would say -- this is just one opinion. I'd say, frankly, there's a reason why we've chosen, out of the funds that I've started, to go the qualified purchaser route. I think the licensure standards are cost-prohibitive for what we're trying to do.

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

MR. BAIRD: Go ahead.

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

MS. PATODIA: Yeah, this is Poorvi. Yes. I just wanted to go back to a comment that was made earlier, and to make sure that I'm understanding what you're saying, but also to talk about it, whether I'm -- someone made the comment earlier that having more individual investors in the market would not help. And I'm curious about that comment and what you meant by that.

MR. BAIRD: Robert, I think -- I think --

MR. FOX: Well, I mean, I guess I made the

comment. I guess I'm just saying that -- well, my concern is, is that with some of the lobbyists and other parties in play that you know, if I think about the big players in the marketplace, if we allow just more individual investment into quote, "private equity" and venture capital and things like that, then some of the large institutional money management firms may just -- you know, we may just get more individual ownership into the larger private equity -- you know. I mean, KKR and some of the other larger private equity firms already allow individual ownership and we may just get more, you know, individual ownership into Andreessen Horowitz and you know, some of the others. Carlyle and some of the other earlier stage funds, right? And so I guess my point is, is that I'm not sure that to quote Chairman Clayton's point earlier, that you know, quoted my 401(k) if I have a private equity option, that that's necessarily going to always be invested into the you know, you know, Kentucky Blue Fin Company, right? It may be invested into more institutional private equity type options, right? That was the point I was trying to make.

MR. BAIRD: Well, when you're looking on the menu, it's Kentucky Blue Snapper.

MR. FOX: Oh, sorry.

MR. BAIRD: And please order it if you see it. It's really delicious. But no, I think your point is well-taken. I think this is the policy question. The goal -- you know, I view crowdfunding and expansion of the accredited investor definition is really a means to an end. And if you guys do a tremendous amount of work and make a big policy change and the outcome is, you know, BlackRock and Carlyle partner to get you know, Maria from Joplin, Missouri to invest in Carlyle, I think that that's not the policy goal. The policy goal, the North Star, should be how do you get more investments in Lula from Paducah, Kentucky. And so I think your point's well-taken that you know, expanding investor base is a tool but not a goal. And policy is about accomplishing goals and figuring out the tools you push and pull to get there.

MR. YADLEY: Ross, do you think it's -- it is a requirement that --

MS. PATODIA: Yeah, I mean, I just --

MR. YADLEY: Go ahead, Poorvi.

MS. PATODIA: Yeah, I was just going to say, you know, speaking as an entrepreneur and a woman who's founded a business and done multiple rounds of financing starting with a seed round and later a Series A round and then two years later a Series B round which I just

closed, and having worked with different types of investors, both friends and family as well as angels and as well as VCs, I mean, I just -- I don't know that -- I don't think that we're -- when we -- at least in my head, when I think about expanding the base of the number of investors that are available, I don't think that it's automatic that the people that we're talking about here, that if they suddenly have the ability to make an investment that they're going to go to these large PE firms and track. Many of those don't even know about those large PE firms, right? So, I guess I'm just saying that that assumption in itself I don't know if that's literally correct. Because I think, when I think about my challenges as an entrepreneur raising money, especially before we were large enough or could demonstrate the types of growth that is required for VC investment, you know, the biggest problem is -- the two biggest challenges are that you don't know where to start. You don't. As a first time CEO, you don't know. You haven't done this before.

And then the two -- the second part is, you don't know who to go to. You don't know who to raise money from.

MR. YADLEY: Mm-hmm.

MS. PATODIA: And the people around you are not -- cannot or do not meet the definition to become an investor. All the stuff about deal costs, all the stuff about, you know, some of the other things that we're talking about, I think they do meaningfully impact the end result, but I don't know if those things are the things that are preventing someone from raising money. Ultimately it is about access to capital, who you can raise the money from and how to do it.

MR. YADLEY: Ross, thank you for being here. I'm on the advisory board of the entrepreneurship council of the University of South Florida which you all support.

MR. BAIRD: Excellent. That's good.

MR. YADLEY: And it's great, and it's been very helpful. I think we have to separate out two very different things that we're talking about. One is the Chairman's desire to allow Main Street investors to have opportunities for investments. So to that extent, getting individual investors into KKR and Carlyle is a worthy goal, and there's no reason that we shouldn't support that and make that easier. The harder one is the access to capital. And one of the hurdles, frankly, is paternalism. And that is a very understandable attribute for a regulator to have to worry about. And you can see in the comment letters that are less

supportive of the concept release than others that people are going to get ripped off by fraud.

MR. BAIRD: Mm-hmm.

MR. YADLEY: And that's absolutely true. It will happen. It happens to accredited investors and qualified purchasers every day and it will happen to middle America investors too. So the way that works best in the marketplace is the Paducah, Kentucky story and a million other stories of local investment.

MR. BAIRD: Mm-hmm.

MR. YADLEY: Because one of the things that the crowdfunding, the way it came down from Capital Hill, didn't really address the local pizza shop that was on the border between Kentucky and Ohio, so the intrastate exemption didn't apply and things like that. There's no way that we can -- and therefore we really shouldn't -- prevent people losing their money. We don't do that in the public markets. We address it by disclosure and independent boards and things like that. And I think that same framework can work. I'm not sure that we can, without a policy initiative, get to the home ownership analogue for businesses where you could cut out the costs and just give people alternatives within that large asset class.

So some of the things we've talked about,

including lead investors and pool investments and things where the lawyer that knew Paducah and really cared, or the entrepreneurs, the professionals in Baltimore that they live there, and yeah, they could lose their money but they're investing in a neighborhood they can see, and they can look people in the eye. And it's the old why general solicitation wasn't -- wasn't available is that people had the opportunity to get the information. So I think the things that we're discussing that will allow people that don't have the time or the expertise -- and it's in -- whatever we do to the accredited investor definition, and I hope we do a lot to enhance it -- it still won't allow everyone to have the individual ability to completely understand what it is they're investing in. So therefore a focus on who invests at the purchase stage, a lead investor or some other mechanism that allows diligence and full disclosure will be a real pathway I think to helping the system.

MR. BAIRD: You know, one -- you brought up a lot of great points. One point that I think about a lot is the risk of fraud does significantly decline when it is local. When there are reputational risks and personal fallouts. You're ripping off a bunch of people that you know and you're going to have to continue to deal with.

And as I think about -- you know, there are a lot of conversations around regulatory sandboxes and pilots. And I do think there might be -- and I think -- and Youngro has been right in this -- Texas and Georgia are two states that have done a lot of experimenting with intrastate crowdfunding with, I would argue, much more success than not, but the local nature has really driven that. I would say if you figure out things like regulatory sandboxes or pilots that are distinctly local, that would be a good thread to pull on. One thing, if you look at the history of, I mean, why the SEC was created was a bunch of people in Kansas City got ripped off by people in New York leading up to the stock market crash. I cited how entrepreneurial activity is at a 100 year low. Entrepreneurial activity in the 40s and 50s is the highest we've seen, and in part because -- and I'm not advocating for a return to this but I think there's an illustrative lesson. Banks in New York, old school folks call them money center banks. And it's because you literally sent your money from Kansas City to Chicago to New York to buy stock. It would pool there. And there was as part of the New Deal a prohibition on sending money from one bank to another. So Commerce Bank in Kansas City, in order to make money, had to find businesses in Kansas City to lend to in order to make money. And so there was a real localization of capital coming out of the New Deal, from a regulatory standpoint.

And you saw immense increases in entrepreneurial activity. And not all of that is attributable to that, but you know, it was post war and boom and all of that. But there is, A, there's a real thread of the things that a regulator might be worried about are mitigated locally. And most money in -- if you -- most money coming from these invested areas is not invested there, and something around that thread would be worth -- worth pursuing.

MS. GARRETT: Thank you, Ross. We appreciate all of your thoughts and comments. And I think that today we're going to follow up on a lot of the different points that you've raised and a lot of the different points that the people on the committee have raised, and it's going to provide a great discussion for our session today. So thank you very much for joining us.

MR. BAIRD: I appreciate it. Thanks for inviting me. And sorry to deprive you of open mic with the Chairman. That's --

MS. GARRETT: I'd also like to welcome Commissioner Peirce, who has joined us.

COMMISSIONER PEIRCE: Thank you. It's a

delight to be here. I spent part of the weekend watching the part of the last meeting that I had missed. And I was just really impressed at the quality of discussion and the efficiency with which you operate. So I'm looking forward to more of that today.

MS. GARRETT: Thank you. The next item I'd like to turn it over to is to Yougro Lee. During our August committee meeting, we created a subcommittee to explore segments of the harmonization release. And Youngro graciously offered to chair the subcommittee. He's going to give us a brief overview of some of the ideas that were discussed by the subcommittee that should form a foundation for our discussion of harmonization and following up on what Ross had to say earlier. Thank you.

MR. LEE: Thank you so much, and thank you guys for really paying attention to this idea. I think it's a really important one that I've personally been involved with as well as several other folks on this committee. I think it gets less attention because we get kind of bombarded by the headlines of the big companies and so on. And we really missed the point which Ross was really great at explaining.

So the subcommittee that we formed, we called it the subcommittee on selling securities over the

internet. And we focused on that, and not these other buzzwords, because as a practical matter, the issues that we're talking about is in fact able to be addressed we think more effectively in the context of online sales. Because if you sell securities online, you are number one, increasing transparency by definition, right? It is much harder to commit fraud, for example, when everything is online for people to check, versus one on one meetings. And that was obviously the definition and the intent for the Jobs Act. The other part was because it enables technology. And when you use technology -- I think some other folks have made this point -- you're reducing the actual transaction costs of doing the deal, whether its in the form of investment agreements or diligence or what have you. And the point of this enterprise -- or let's just say this industry of online securities sales, as guided by the SEC and the Jobs Act, was in fact the system that Congress and the SEC tried to institute to help address some of these issues that we are talking about today.

So the subcommittee members, I really want to thank Sara Hanks, Catherine Mott, Jason Seats, Hank Tobert and Greg and Mark from the agencies, as well as Carla and Jeff, who participated. We met several times or virtually met and talked over it several times since

the last meeting, including just really critically thinking about these issues. So I'm just going to highlight a few of the items that we agreed. Actually it's on this list right now, so I'll try to summarize into these five points. And I think throughout today we'll be discussing each of these topics a little, a little further.

So the first was -- and we summarized in words here, but I will just give you the full phrase. SEC should cease regulation of offers and focus only on the actual sales of securities, since there is no practical harm caused by mere offer of investment opportunities.

Well, the first thing is harmonization. I mean, that is the catch all for everything. So harmonization will be basically going off, going off based on the SEC harmonization rules and then kind of summarizing all these things we talked about. The second point was the regulation of offers and sales that I talked about.

The third point was the definition of accredited investors. And essentially, to encourage participation of more investors into the startups and small businesses that we're focused on, by changing the definition of accredited investors.

The fourth point was really the other side of it, which is the non-accredited investors. Regardless of how you define accredited investors, there's always going to be a group of people that are not that. So how do we help these investors access? And that is in the construct of Regulation crowdfunding and Regulation A, which literally is the mechanism that is in place. So we don't need to invent new things. It's been in place. And the issue, the more practical solution that we're trying to come up, how do we modify at least some parts of it, so it's not something starting from zero.

And the final point really is about the pooled investment. And the issue of gatekeeper obviously overlays everything we just talked about. But how do those particular concepts interlay? How does, for example, pooled investment funds -- could that be -- I don't want to use the word "compromise" but could that be at least one solution that addresses both the business focus on trying to bring access to the capital, as well as investor protection concerns?

So, that's a summary of the major points that we discussed on the subcommittee. And again, I'm really grateful for Carla and the committee for giving us the opportunity to discuss these in detail.

MS. GARRETT: Thank you. And I will say that the subcommittee kind of evolved, not only talking about

selling securities over the internet, but then we became just talking about the harmonization release in general. And so, a lot of the points we'll be talking about today don't necessarily fall into just selling securities over the internet, but they do fall into just the harmonization release. I'm just going to kick it off. What we're hoping to have between now and lunch, which will be in a little bit over an hour, is a pretty broad discussion on different aspects of the harmonization release. We will also have time this afternoon to continue our discussion. I'm going to kick it off on the very high level of just what the harmonization release is conceptually.

You know, the SEC took a broad review of the available exemptions and they seek from us our input, in order to assess whether the current exempt offering exemptions are consistent, successful and effective for small businesses wishing to raise capital.

A couple points to note is that the current exemptions have a variety of very diverse requirements. Some limit the amount of securities that may be sold. Some limit the manner in which they can be sold, so that there's no general solicitation. Some exemptions have information disclosure requirements. Some don't. Some exemptions limit who can invest, so that only accredited

investors can invest. And some exemptions limit the amount certain investors can invest, and some exemptions don't.

And the commission has asked us as a committee to provide input on this exempt offering framework as a whole, and whether or not we believe it could be more concise and less complex. And they've also asked for our input on specific conditions that -- to each of the current capital raising exemptions, and whether those exemptions are appropriate to helping small businesses raise capital.

I'm also just going to provide a really brief introduction to 506, because 506, as everyone knows, under Regulation D, is the most commonly used private placement exemption. And I would say in my experience, it's used not only by companies seeking large amounts of money, but it's also used by small, small companies obtaining smaller amounts of money. And if you sell to only accredited investors in 506(b) then you can have an unlimited number of accredited investors. There's no limit on the amount of money that can be raised, provided that there's no general solicitation or advertising, and they're not subject to specific disclosure requirements. If you include one non-accredited investor in a 506(b) offering, then you now

have information disclosure requirements. And the rule under 506(b) states that you can have not more than 35 non-accredited investors.

I think that a lot of comment letters have discussed how it is costly to bring a non-accredited investor into a 506(b) offering. And so I think that that would be a good thing for us to discuss today. Also a lot of the comment letters talked about how 506(b) is working for accredited investors in its current state. And so, if we look at 506(b) we might want to think about maybe whether we change it or whether we keep it as is and we broaden it in different aspects.

I just want to also note 506(c) which is where an unlimited number of accredited investors can also invest, but there can be broad general solicitation in a 506(c) offering as long as all of the purchasers are accredited investors. The one issue with the 506(c) that has come up is that an issue owner has to take reasonable steps to verify a purchaser's accredited investment status. And if you read the comment letters, it becomes clear that issuers also often don't want to take these steps or find it burdensome to take these steps. So 506(c) is not being used as much as 506(b).

With that brief introduction, I wanted to open it up to the Committee. I want to also point out that we're going to -- we could simultaneously have -- I think Catherine was willing to talk a little bit about the accredited investor definition. All of these items go together. Because if you -- if you tweak the investor, accredited investor definition, then that means that more people could fall into the 506(b) category. Sarah is going to talk about whether the offer should be exempt, and that definitely can impact whether or not general solicitation comes into play. And when we get, later on this afternoon, into the pooled investments, that can be a great way to get non-accredited investors possibly into the market. And Youngro is also going to be discussing Reg A, Reg CF and other ways to get non-accredited investors into the market. So with that, I'll open it up to the committee.

COMMISSIONER PEIRCE: I'll just start just with one observation, just to reflect what you were mentioning about the comment letters. In our office, many of whom are seated right here today, when we have been out and about and leaving D.C. and talking to businesses and investors, one of the things that we consistently hear is one, a reflection of the local nature of investing and how most capital starts out local. You may move into raising capital from those who

are further away that don't know you. They don't know the business. But it tends to start more locally, which our speaker just conveyed. But one thing I'll just say as a starting point as we talk about the framework, kind of terrible analogy, but I love terrible analogies. They've kind of become one of my favorite things. Is if you think about, we have a garage full of different types of vehicles. You have everything from bicycles to motorcycles to maybe a golf cart and then a car, and each of them can take you to different destinations at different speeds with different capacity load. I think that there's a lot of people who, as they look at it, they see problems with each of them. They see that the, you know, the speed regulator on the motorcycle, they wish you could take that off. They might wish that you could put, you know, a carrier seat on the back of the bike to bring an extra passenger along. But they're very worried that you're going to mess with the family vehicle that they use day in, day out, and the one that is consistent and that has been a reliable resource. And that's something that we have heard reflected.

So as we think about the tools that are available, I think it is important to think about, not only as we were talking earlier about kind of the top down size of the funnel and the capital that goes in but

also the bottom of the funnel and where the money is going out. And how companies start out raising capital and then how they scale in to other sources of capital, and making sure that we don't have kind of a singular angle view, nor are we looking at only one of the vehicles that is in the garage, and instead thinking about all of the different tools that are available, because they do have different utilities, and making sure that they're all optimized, so that different companies and investors can get to their destination efficiently and effectively. So that's just a reflection of what we've been hearing. I thought it would be important to share it. It backs up a lot of what we've seen in the comment letters.

MS. GARRETT: Very well said. Thank you, Martha. Catherine, would you like to talk about the accredited investor definition?

MS. MOTT: Sure, I'd be happy to. I was planning to sort of introduce this as the accredited investor definition, which is a central component of several registration exemptions. It serves as a proxy for an investor's financial sophistication and ability to fend for itself. Accredited investors have significantly more access to the ability -- or more access to a wider range of investment opportunities,

compared to non-accredited investors. Therefore, the release -- the harmonization release solicited input, among other things, whether additional categories should be included as accredited investors, whether existing financial threshold requirements should be adjusted and whether alternative sophistication measures should be used to qualify investors as accredited. And whether a broader range of investment opportunities should be made available to non-accredited investors. So I'm going to give you some thoughts that might even -- not might but will reinforce what Ross has mentioned already.

It's well-known by economic development professionals and economists that all net new jobs in the United States are created by companies five years old or less. And accredited investors play a key role in this. And I think Martha was just mentioning this about talking to the local people and how much more they are involved in the early side. So accredited investors, now known as angels, provide 90 percent of outside equity for the early stages of company development. On average, annually, they invest in 70,000 new companies, somewhere around an annual average of $25 billion a year. Now, just for perspective, venture capital provides most of the later stage capital. That assistance scaling the company, around 7,000 to 8,000 companies annually, but around $70 to $80 billion annually.

But unlike venture capital, where 80 percent is deployed in California, Boston and New York City, only 45 percent angel capital is concentrated in those three locations. The remaining 55 percent is invested in flyover regions. And as you heard today, angels invest in their own backyard and are very active in regions hurt most by structural changes, like the demise of manufacturing, loss of jobs due to automation and in regions recovering from the great recession.

These angels are not investing in Uber or WeWork or other such unicorns, but are investing in companies like Wombat, Inc., which was a cyber security -- which is a cyber security solution which started with five employees and can now account for over 300 plus employees. The Angel Capital Association supports expanding the pool of angel investors to include those with professional experience and professional certifications like CFA, CPA, MBA, JD, Series 7 securities. They're just a few examples to consider. The education and experience of such individuals can easily assimilate the information required for sound investment decisions.

Also, the ACA recommends a "do no harm" by

retaining the financial criteria for an accredited investor and leaving the thresholds unaltered. If the income and net worth criteria are increased, the flyover regions of our country will be hurt the most. Cost of living in Saint Louis, Missouri cannot be equated to the cost of living in New York or San Francisco. A $200,000 annual income in Saint Louis likely equates to $450,000 in New York City, and a net worth of a million in middle America is likely to be equivalent to about a $2.5 million net worth in New York City and San Francisco. And most importantly, nowhere in our country is investment more needed than in middle America. It is imperative that we don't damage the ecosystem that is helping distressed regions slowly recovered. An example of such stories are prevalent in Greenville, South Carolina, Detroit, Michigan, and Saint Louis, Missouri. These regions have active angel groups investing in startup and consequently are even attracting VCs looking for opportunities in underserved cities, like Rise of the Rest.

If the thresholds are raised to the Dodd Frank recommendations, the Angel Capital Association as well as the OCC have previously estimated a reduction of about 60 percent active accredited investors. I say active, not qualified, active. The ones that are

writing the checks. One of the things we think -- we don't know for sure but we think -- is that the reason that these -- that individuals are willing to risk their capital on the lower wealth spectrum is that they're interested in gaining more wealth. They're willing to risk some to gain more wealth. Whereas those who are at the upper end or in the -- they're in family offices. People are managing their money. They're all about thinking about how do I retain this wealth, versus how do I create more wealth. So that behavior of active accredited investors tend to be on the lower end spectrum.

A 2017 McKenzie study on the future of work suggests the following: sustaining robust aggregate demand growth is critical to support new job creation, as is support for new business formation and innovation. Fiscal and monetary policies that ensure sufficient aggregate demand as well as support for business innovation and business investment will be essential. It behooves us to expand the definition and considering that a one size fits all is impractical for regional economic dichotomies. Furthermore, China has gained significant ground at a remarkable rate in advancing innovation and encouraging capital investment in multiple sectors, and the United States is falling

behind. So I hope today we can deliberate on meaningful changes to mobilize more investors and accelerate the economy of the United States. But I do -- and I do see the 35 unaccredited investor definition, the additional disclosures is, I think, a problematic issue for advancing this.

MS. GARRETT: Thank you, Catherine.

MR. SEATS: In terms of trying to make progress and structure that conversation, just something that's occurred to me just sort of reading through notes on the comment letters is there's really a couple different baskets of change that are being proposed. And so I'll throw out how I think about it, and it may help, it may not. One are what I'd think about as maybe incremental changes to the existing definition. Examples are things like, including you know, primary residence towards the net worth calculation, or moving towards percent of net income for you know, versus, versus a wealth or a dollar, right? So the -- so, like, those are sort of minor changes. Then there's a whole set of the recommendations that fall into the category of testing for sophistication in a different way, either because it's a knowledgeable employee or some sort of testing or some other framework. And then there's a whole other category which is assuming accreditation under, because of the circumstances of how you're investing. So either because the vehicles that you're being pooled into have either direct or indirect regulatory regimes that provide investor protections, or there are co-investors who are investing on same terms alignment who are sophisticated. I think of those as sort of three different paths. I mean, I don't know if, where the viewpoint is in the room on which ones feel like no brainers, which ones there's a lot of work to do or if there are other categories besides those broad three.

MS. MOTT: So one of the things, Jason, had I not lived through the Great Recession here '08, '09, and I was actively involved in a business and saw what happened -- when they did add the -- you know, or eliminate the value of your home as net worth, I would not add that back in. I would not. I would say a residence should stay excluded. And even before that was excluded, when people would join our group I would tell them hey, your financial advisor recommends that this asset class should be no more than 10 percent of your --

MR. SEATS: Right.

MS. MOTT: -- investable assets. And I say, your investable assets. Your home is not an investable asset. So I'm reluctant to, you know, to say oh, yeah,

let's put that back. And that's just because I -- you know, I saw what happened with the Great Recession. I will tell you this. The more resistance there is to -- I guess to validate your sophistication, I think the less people you'll get involved. I mean, a good example of that is 506(c). Because there's so much that you have to go through to verify, and like every quarter. And you're trying to build a portfolio of 35 companies every quarter, and the companies are back raising another round. And I mean, that's why people don't do it. The more resistance there is -- I mean, that's human behavior -- the less likely they'll participate. So if we have a -- you know, right now you self-certify. And if you include in there, you're not an accredited investor but you have a check mark that says, I have one of these certifications, I'm a JD, I have a Series 7, whatever, I think you'd be inclined to get more people involved. A sophistication test, maybe.

You know, I think about the example Ross was talking about, an individual who is an attorney making $100,000 a year. Would that person bother with you know, with a sophistication test? I don't know. Would we get a greater number of people to participate if we didn't? So that's one of the things I would encourage us to think about it, is the more barriers we create

because we're trying to protect people -- and I get it, protection is important -- is that the less people will participate. So how do we find a balance there that allows us to say yeah, this person has reasonable expertise without having to go through, you know, jump through several hoops. Because that is -- in my opinion, that's what's prevented 506(c) from being more successful.

MS. HANKS: Could I just weigh in on this whole 506(c) and 506(b)? Some of the barriers that Catherine is talking about are not actually barriers that the regulations or the staff put into place. A lot of it is interpretations -- and sorry about this -- by the lawyers. And I think one thing that the staff could usefully do is revisit the whole self certification is okay for 506(b) trope, because it doesn't actually -- when you talk to the staff, the staff will say we never actually blessed that. And we do see in this whole market this whole check the box mentality where everyone is like 506(b) all I have to do is check the box. I don't even have to spell my name right. And 506(c) you've got jumping through all of these hoops and you've got the safe harbor and the lawyers are pushing the safe harbor you've got to get recertified every quarter. The law doesn't actually say that. And so some kind of

pronouncement from the staff on the -- we never said that with respect to (b) and we never insisted that with respect to 506(c) would in fact be very useful. And sorry to throw it back on the staff.

MR. LEE: Can I just -- just one on the topic, because it's really two points. We are a platform that in fact do 506(c) offerings, and exactly the point -- I agree with Sara. But because of the way the world works, we literally require people to submit their tax forms, get a certified letter from their accountants, and we have to check it every six months or three months or whatever that test is. And we literally have investors that I know personally is an accredited investor because they're a member of the angel network. They have literally invested in some other things that you know -- you so, so forth. And they frankly don't want to give us their tax forms and their income statements and so on, so forth.

So I think this is a very critical point to make clear. Because right now every single 506(c) offering, at least the platforms that are doing it right -- that's an issue with gatekeepers that I'll reserve for a later discussion -- the platforms that are doing it right are penalized by trying to be more compliant, better for regulators and investors, so that's a very critical issue. But the other main point that I want to just emphasize is the issue of risk. Like there's a -- I don't know what's driving it, necessarily. It may political. I'm not sure. But there is -- there seems to be this bias that risk is not good, right, for an investors, frankly. But the entire purpose of the securities laws, especially private placement, is that no, we want -- we are willing as a system to provide the investment risk to individuals who are understandably willing to take that risk.

So like when we -- this is an earlier point that I said earlier, when I talk about small businesses which is often food and beverage or more retail, they just say that's just risky. I'm like what does that mean? Because risky is if you're getting nothing for a very risky investment. If you're getting, you know, just making this number of, 15 percent returns, or 25 percent returns or even -- at least you're targeting for that risk, I'm sorry, that return. There is a commensurate amount of risk that is being provided where people are trying to -- individuals are wanting that risk.

So I think if you keep that principal in mind is, risk is not an inherently bad thing. The bad thing is if you're not pricing that risk well. I think that's

an important point, because when I come back to, and how it relates to this question that Jason asked, is, is through the sophistication and certification, however you define it -- because there are so many individuals that are generally younger. The example that Ross said was the young lawyers in Baltimore who presumably know what they're doing, especially in their back yard. But even in these professional private equity firms that we think are -- every single of their analysts and associates and VPs that are doing the actual work, I guarantee you, 90 percent is not -- is not accredited investors, but they are the ones that are actually analyzing investments to decide whether this product -- we manage to make the investment or not.

So it's just so -- to me there's a big gap in what we consider risk and what we consider the qualifications to asses that risk. And clearly it's not how much money you have; it's what you know. And so my, I guess, if I can make a suggestion, would be to definitely include some sort of whether it's a sophistication or certification test, based on whether your prior performance or education necessarily, whatever it is -- because right now the accreditation on income or net worth just doesn't reflect the ability to assess that risk.

MR. SEATS: Just one minor clarification.

MR. YADLEY: And --

MR. SEATS: When I said this sophistication test, I meant that broadly, not specifically here's the test to take. But I think it's a spectrum of what is the criterion by which you measure sophistication. The most lax version that was in a comment letter was just requiring the non-accredited investor to opt in and claim that they have sophistication, which is in many cases what's happening on the public market side for retail investors. And so I think it's a spectrum, from take an actual test, get a you know, certification, to I'm acknowledging that I can lose all of my capital and this is a self-certification test, right?

MR. YADLEY: I think this is a public policy -- isn't there really a public policy matter there that's more like, you can't absolve people -- you can't just wave a magic wand and have people absolve their right to pursue remedies if they feel like they've been, you know, mislead. I mean, the issue -- and just going back to something that Catherine said, I think one of the issues around interpretation from lawyers are all about you know, protecting yourself from the plaintiff's part, frankly. It would be helpful if the SEC gave guidance. But most lawyers I know ask us to do things to

basically put rails around ourselves to be protected in some way, shape or form from lawsuits that will ultimately be arbitrated on, you know. And so that's, that's sort of where I think that comes from. Let me ask it a little bit differently. Is there a general way to go at this and maybe think about, again, looking for regional investments? So is there a way to think about creating exemptions to the existing rule based on geographical participation? I'm going down the thread of, people are less likely to -- the strong desire seen from our speaking this morning, and from what I've heard from a number of people is that there are a number of individual investors who want to be able to invest in their own communities and businesses they think they know well.

And so I'm wondering if we -- if we thought creatively about it, say creating a 20 mile radius or a 25 mile radius or something in and around the investable area, is there a way to carve people out of the accredited investor based -- if they have a geographical test there is a presumption if you are investing -- if you live in an area and you are investing in a business in that area, that there is a presumed level of sophistication that essentially allows you to invest, without you know, pursuant to an example from 506(b) or

(c) or whatever those are. Is that something that anybody else has thought about?

MS. HANKS: I think -- this is Sara. I think that the more you do that kind of thing, the more you make it complicated and the more you create incentives for people to just check a box and lie. Yeah, I lived there. Or why are you not including me, because my grandfather lives there and I go there every weekend. So I know that place. I mean, the more different categories we create, the more incentive we create for somebody to go around it.

MR. YADLEY: The sophistication knowledge point, I think the best way to start addressing that would be to be very clear about what it is that we're quote, "testing" for, or whether there's an actual test for all these other things. So for example, since I have a JD, I'd be happy to become an accredited investor on that account, because I don't have an MBA. But on the other hand, law school doesn't teach you anything about management and reading financial statements. So I think the knowledge, sophistication really ought to be on those things that are common to all businesses, and then leave it to risk factors and disclosure to talk about the specific business. You could then get more specific and say for banking and financial and FINTEC investments

then maybe there'd be other categories. Again there's the worthwhile goal of including more people with corresponding complexity that Sara just mentioned, that you could become crazy figuring out, now which of the categories of sophistication am I going to fall into.

MS. MILLER: I was just going to add one note to Jeff, to your question about the regional investing exemption. We do have the intra-state exemptions, and states have been left to craft some of their own rules and frameworks, many of which allow participation by non-accredited investors. I think Mike could speak for hours about the different tools and ways that states have done it and companies that have famously -- like Ben & Jerry's raised capital in his own state. But that is a framework that exists. It's not based on a mileage radius, but it is looking more at activities which happen within the framework of a state. So that does exist as one option.

MR. PIECIAK: Martha, maybe I could just use this opportunity just to say one point I wanted to make about this discussion generally and talk about something that we did specifically in Vermont with our intra-state exemption. So we do allow for something that we dubbed a certified Vermont investor, which is basically half of the accredited investor financial requirements, and we

allow people to invest more than the cap for a normal retail investor. But we do put a cap on it of I think it's $25,000 that they can invest. So I just mentioned that concept that we put into place in Vermont as part of this larger discussion about the accredited investor test is there to show sophistication or a proxy for sophistication and also the ability to withstand the loss as well. So I think that ability to withstand the loss is equally important for, if we're talking about opening up the definition to allow individuals in that maybe don't have that same ability to withstand the loss, then think about other protections that can be put into place to prevent something that we don't want to have happen. So whether it's a cap or a percentage or something like that. That's something that we've put in our comment letter and talked about and something I just want to raise here.

MR. FOX: I think that's a good point. Because I'm a little confused as to what the point of the discussion -- right? I understand the protection aspect, but I feel like we're talking two different things, right? Sophistication, everything else, right? I mean, I mean I feel like on one side we're talking about okay, do you understand you're investing in something that you could lose all your money, right?

That's a risk decision, right? You know. The other thing is, do you even understand what the business is you're investing in, what it does, you know, how it works, that sort of stuff? That's a -- yeah, I mean, some of the things I mean, you could need to have a, you know, molecular biology degree. Who knows, right? And I don't know any regulation you could, you know, anticipate all the various needs. And so I guess I'm trying to understand, when we talked about sophistication, you have to actually understand what the business is doing, or is it just simply you really have to have an understanding that you're making a risky investment and you need to -- you may lose all your money. And yeah, I mean, I don't want to -- I mean, I know it's more complicated than that. But I feel like we're talking -- people are making different arguments or variations of both sides of those arguments, and so I'm not even sure we're saying the same thing around the table, so.

MS. MEHTA: To -- you know, on that point of sophistication, one, how many more accredited investors will that bring to the table, if we were to have some sort of test for sophistication? And also, you know, it would be a little -- while it makes sense directly of why you would allow people with certain financial sophistication levels who have passed certain exams or lawyers to, you know, as that, to serve for those degrees or you know, certifications to serve as a proxy for accredited investor status. But on the other hand, you know, there are a lot of smart people out there. There are neurosurgeons and other fields that could just as easily read words. You know, they can go through and read documents. So like, where are you going to draw that line so that it's not an arbitrary line and it's not deemed to be a little self-serving when the SEC allows just lawyers and people with financial degrees to be able to make investments in these companies. Because oftentimes when you're doing diligence on a company it's more than just financial statements. It's more than reading the documents. A lot of times you need to understand, what do their customer contracts look like? Are they still in pilot phase? Do they have recurring revenue? You know, there's just a lot more. Maybe it comes down to real estate leases. So there's a lot of sophistication you might need to know, and it's not necessarily legal or financial. So, I -- I don't really see that as being a useful test.

And then on the accredited investor, you know, what else could you potentially do? I mean, is there -- maybe we could just have a bright line rule. Instead of

it being, you know, a percentage of net worth where you then have to provide all these documents to prove it, is there any comfort around saying maybe like some dollar threshold, where anyone can invest up to $10,000, period? And that, that comes with a list of risk factors, including, you know, that they may incur losses, they may have certain tax impacts, depending on what sort of entity they're investing in, particularly if they're going to receive K-1s. You know, they need to know that up front, because that's not something most people who don't -- who aren't in the business of investing, they don't really know that. So maybe like a healthier set of disclosures, but without being burdensome to the company, you know, to come up with a list of, you know, audited financials and all the other information that they're currently required to provide to non-accredited investors.

MR. SEATS: My general take on the sophistication discussion was really -- at least from an affirming standpoint was, are we even barking up the right tree? Is it the right thing, category of measurement to be thinking about? And there's managing the risk of loss. That's a whole -- I mean, it's related still, but just sort of related, versus aligning interests with others who we seem to be totally fine

with what their behaviors are, right? I mean, I feel like it's an important comparison, and I'm not steeped in these regulations, and so I don't know the nuance. But my perception is that a retail public market investor can put all of their net worth and more at risk readily without any sophistication test. You just check boxes and whatever, but you can go create levered positions and trade in exotic derivatives by just getting on a trading platform and clicking some boxes. And so we don't seem to have the same level of paternalism in that market as we have here and I don't know why. And maybe my instinct on why is that the fundamental underlying asset is more volatile.

When you think about large public companies, like yes, you can make investing in Google be an extremely proposition, and you have to, yes, you need someone to sign off on yes, I could lose all of my money. But if you're just buying shares of Google, your changes of losing all of your money in the next year are relatively low compared to putting that same $25,000 -- right?

MR. YARDLEY: Well, I just -- well, so, yeah, so part of the answer is -- and that really goes fundamentally to what used to be a very bright line dichotomy between a public offering and a private

investment was, at the public offering of course, you do have all of this superstructure of disclosure including ongoing disclosure and at the front end you have the SEC and the states reviewing the disclosure. And in the case of two-thirds of the states, really making a decision about whether this is a good deal or not. And of course Google was not a good deal in Massachusetts. So it's all a proxy for that. So this paternalism is there because you don't have the government looking out for you. So the question is, where do you put the fence? And nobody believes that having a million dollars equates to sophistication, but it's worked. It's worked since 1982 as a bright line. And there's a little bit of well, if you have a million dollars, unless it is all your wealth -- which it shouldn't be, because you're supposed to have other assets and you're supposed to know who it is that's investing -- the -- and so I think that the $10,000, that's a great idea, anybody can do that. But that's sort of what crowdfunding is supposed to do, and that has all the other issues about cap tables and so on.

In answer, Robert, to your question, I think what I was trying to say earlier was yes, this knowledge qualifier or sophistication qualifier should be really basic, including can you read, can you understand what a financial statement is, and not a whole lot more. Because the more you get beyond that, those basics, the more it depends on the deal. I have chartered, as a lawyer, I don't know, 20 banks in my life and I represent lots of banks, and I'm a shareholder of many large banks. And it's not an understatement to say that I don't understand the footnotes of those financial statements that go on for 100 and some pages. And so, yeah, I'm very sophisticated and I know how to read these things, but that -- and the other part of this is, and this is why some of the -- well, the fact that wealthy people invest in private equity funds is, a typical private equity fund looks at 1,000 investments, and they seriously look at a couple hundred, and they diligence, you know, dozens, and they make eight or ten investments a year, and a lot of effort goes into that. And as an investor who has a day job, as the Chairman says, you can't do that. So you can't really protect yourself. So what are the fences? And one is, if it's not going to be a registered offering disclosure for purchasers. I think that's where you start. And then for less sophisticated people, since we won't be able to get away from investor protection nor should we, who is helping them? Is it a registered professional? Is it a lead investor? Is it -- some of the comment letters

talked about if at least x percent of the investors are accredited then you should be be able to have unaccredited investors who are riding their coat tails.

So it's -- it's going to be complicated however we get it. But we've got to get past the point of -- as I think Youngro and others have said, I mean, there's risk, and you could lose your money. So we can't overemphasize that that is a possibility. And so the investor limits, you know, they're fine, but those certainly could be harmonized. There's no reason that they should be different, with the different quasi-exemptions like Reg A and and CF.

MS. GARRETT: Oh, go ahead.

MR. SOLOMON: Yeah, I also think that they're different, the public markets, the private markets. Because with the public markets, in many a case, you're coming into through brokerage firm and there's this intermediary there that's being held to a standard. And you know, they have to take on through this whole thing with Reg BI, and they actually have a fiduciary responsibility and that's seen. And there's all this financial protection. You're much more towards the intermediary, for appropriateness of investment, the length of it. Even when you open up a sub Forex sub

account where they let you trade for free, news flash, but when you -- when you get something for free it kind of means you are the product. News flash.

But you know, the amount of forms you have to fill out are -- sorry for the sidebar. But the amount of forms you need to fill out and the things you need to do in order to get access to the public market vehicle are discrete. In here what we're seeing is, you know, there is no free private investment. Well, nobody's an intermediary. And maybe that's one of the things that should be faced.

Maybe we should be in a position where we hold the intermediary or fiduciary responsible for helping to create the transmission of capital from a small individual investor to a small private company. I mean, again, I think we offer two things here. One is unlocking the flow of capital for small businesses. The other is unlocking the flow of investment opportunities for small investors. And I think a third thing is -- and I heard this loud and clear -- you don't have to go through New York to get everything. I mean, that's the thing I just heard, you know, very loud and clear from everybody that spoke, right?

You know, if you're in Austin and you want to make an investment in Austin, why do you have to go to

New York to get approvals? And that's sort of the fundamental problem, as you'll find a lot of the capital continues to sit at the -- at the coast. And so if we could figure out ways to exclude the coast in this decision while creating investor protection. So you know thus far, I think maybe there are some things to do re: that. Or maybe there are some things to do by holding, you know, fiduciaries accountable or responsible for effectively screening. I don't think for a second that individuals are capable of screening private or public investments by themselves. And they will lose money, and it will be a huge issue. I think it's been a big impediment to why crowdfunding hasn't been done more. I don't know. That's sort of a response, but also a continued to push towards trying to come up with creative solutions for getting, you know, small private investors involved in the mix here.

MS. GARRETT: Thank you, Jeff. Catherine?

MS. MOTT: I was going to say --

MS. PATODIA: This is Poorvi.

MS. GARRETT: Poorvi?

MS. PATODIA: Yeah, it's me. I was just going to add, you know, I -- I do agree that investors need protections, but as it relates to the definition of an accredited investor, I would say that's -- he says that just because you need the definition of an accredited investor, that means that suddenly there are more protections for you or that you are going to somehow protect yourself, versus someone else who may just fall short of that definition. So I guess I'm just saying, you know, it doesn't feel like those investor protections are there. And so I think we all agree that they need to be there. But the definition of an accredited investor we're seeing today is not -- doesn't seem to be really providing that protection. And so I think these are almost two different issues.

MS. GARRETT: Thank you. Catherine?

MS. MOTT: So one of things I keep -- that I hear -- it seems here all of us agree on is that you know, we need to be able to acknowledge and sustain the risk of losing all your money, so, in that, so. And I get where we're at. You know, in a way I think we're thinking at this on a global perspective as a, you know, as if we're funds and we can -- you know, in a sophisticated fashion assess the business risk and do the four pages of due diligence and the technical due diligence and all of that.

I will tell you that even the best fund managers don't know all of the risk. It's new business models. It's things that we've never seen before

sometimes. The science of it can be very, very complicated to understand. So at the end of the day it comes down to do you understand and can you sustain that risk. Secondly, though, I don't want us to overlook the value of the local people who know the person who's building that company or putting that, you know, team together. And it's going to make a difference in their community and their ability to invest in that, because they don't make enough money, to take that away.

I just think about the -- my little hometown that I went to, and went back to, and saw this you know, group of people who got together. Now they're all accredited. But imagine if -- and I guess the other thing I think about is, when someone is in need in that community, they know how to do a Go Fund Me page, and everybody comes to their need and they're putting money in. And imagine if it was that simple for them to say look, we can restart this.

There's a group of these accredited investors who are trying to put their money together to invest in this aluminum extrusion restart so to speak. But you know, imagine if some people could put a little bit more money in to help their community and invest alongside of those accredited investors. And they're not accredited, but they can take that risk, a certain amount of risk,

to say that could be really meaningful to me. I own this, you know, little grocery store, and I could, you know, put a little bit of my money in that aluminum extrusion plant, knowing that I'm going to get more customers later on, because we're bringing -- we're attracting new jobs. We're attracting -- you know, I'm just -- what I want us to do is I want us to find a happy medium on this. But not forget about the 55 percent of the country that is not getting venture capital. Is not -- you know. Needs that kind of injection in the arm. And also, let's think about -- we're talking about who do we add, what -- how sophisticated they are.

But also we're not talking about, you know, the thresholds and what that means for those regions. I want us to be very mindful of the fact that you know, someone in the little town of Greenville, Pennsylvania, of 5,000 people, is not going to be the same as someone in New York City, that's what, 50 million? I don't know the size of it. But let's just be mindful of that, that we don't create things that make it more difficult for the -- for middle America to be successful. That's where I'm at.

MR. TORBERT: Can I --

MS. GARRETT: Thank you.

MR. TORBERT: Go ahead.

MS. GARRETT: I was just going to say, if I can -- we have a lot of things to talk about. I want to pull together some of the thoughts that we have explored. First of all, Jason, I think that you did a good job outlining the different tiers. One is for the accredited investor definition. First of all it's what are the financial thresholds. What I've heard, you know, Catherine say repeatedly is let's leave -- do no harm by leaving the current accredited investor financial thresholds in place. That's one point. The second point is, is can somebody become an accredited investor by -- because they are sophisticated? And in this aspect for it, I think what we're talking about is sophisticated as the person, and not sophisticated, necessarily, about their knowledge of the company. But it's somebody --

MR. SEATS: Carla, on that -- on that first point, one thing I did hear was, is there room for localizing that?

MS. GARRETT: Right.

MR. SEATS: Because not all markets are the same.

MS. GARRETT: Okay.

MR. SEATS: Yeah.

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MS. GARRETT: I'll add that to it. So on the second point about sophistication of an individual, as a committee, we maybe don't get into the exact definition of what that means, meaning is a JD, is it an MBA, is it a Series 7 test? But as a committee, are we in a position to recommend that possibly the SEC could consider sophistication of the investor in determining what the definition of an accredited investor is? And that would be a way to narrowly expand the definition of an accredited investor.

One of the other points that was brought up is, should a test be a possibility? That could be something that we think about. Another possibility was opt-in although I am not hearing that that is necessarily what people are in favor of.

And then the third thing is --

MR. SEATS: Wait a minute now. I had one on that one.

MS. GARRETT: Okay.

MR. SEATS: Which is to mirror the level of diligence that happens on public market investors having access to exotic derivatives as an example. Which is just me going through clicking enough boxes that I understand it's highly levered and -- because I view those as similar. It's a way to turn that Google

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investment into a very, very risky investment.

MR. TORBERT: Or Forex.

MR. SEATS: Right?

MS. GARRETT: Yes.

MR. SEATS: Yeah.

MS. GARRETT: Yeah.

MR. SEATS: Or Forex is an example, yeah.

MS. GARRETT: And the third thing that you mentioned was how do we get investors to be able to invest alongside accredited investors? And so to me that's actually kind of a third category, because that's not putting people into the accredited investor definition, but it's allowing non-accredited investors ways to invest. And that would be by crowdfunding, Reg A and also by what we're going to talk about this afternoon, with pooled investments.

Do we have any consensus on the definition of an accredited investor and whether or not the committee believes that we can make a recommendation to the committee with respect to the accredited investor definition? My proposal might be is, you know, do no harm by leaving the current accredited investor financial thresholds in place, subject to looking at them for different regions and possibly lowering them in different regions. And for the commission to look at

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revising the accredited investor definition to allow individuals to qualify based on other measures other than financial thresholds, such as sophistication, which the SEC could come up with how they define sophistication. Possibly professional credentials, work experience, education, and possibly a sophistication test. May I get the committee's input on whether that would be a recommendation that they approve?

MR. FOX: There was one other thing that I --

MS. PATODIA: What was the -- what was the other -- the opt-in?

MS. FOX: Sorry.

MS. GARRETT: Yes, Poorvi, what was that? I'm sorry. Go ahead.

MS. PATODIA: I was just asking -- you mentioned that one of the -- one of the options that was discussed was an opting-in mechanism. And that there doesn't seem to be a lot of support for that from the committee. What was that option? What were you guys thinking about for that?

MS. GARRETT: I think the opt-in provision is really just where somebody checks a box and says that they are opting in to be an accredited investor and that they accept the risk. And they might not have a sophistication -- be, necessarily, a sophisticated

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investor by definition, and they might not necessarily meet any of the financial thresholds, but they are opting in to accept the risk and invest in an investment.

MS. PATODIA: Got it. Thank you.

MR. FOX: The only thing I was going to say is I think somebody threw out the idea of potentially, in lieu of maybe a sophistication or in addition to maybe having just like a up to $10,000 threshold that you could just make an investment. I'd be willing to also have that as part of the recommendation as well, or something like that.

MS. GARRETT: So what I was saying --

MR. FOX: Yeah.

MS. GARRETT: -- that would fall outside of the definition --

MR. FOX: Okay.

MS. GARRETT: -- of an accredited investor.

MR. FOX: Okay. Got it. I didn't want to lose --

MS. GARRETT: Right, no.

MR. FOX: -- the sight of that either, so.

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

MR. FOX: Yeah.

MS. GARRETT: I just think it's a separate piece of the puzzle.

MR. FOX: Okay.

MR. SEATS: There was a set of comment letters. This is not pooled vehicle, but there were -- the comment was to allow unaccredited investors to be deemed accredited when relying on investment advice of financial professionals that have demonstrated sufficient knowledge, yada, yada. So I -- that's slightly -- that's another -- that's sophistication by proxy, perhaps. I don't know. But I just wanted to -- I don't think that was spoken out loud. It's different than a pooled vehicle. But it was in a lot of the letters also.

MR. YADLEY: Yeah. That was one of the things I was thinking about. I think that falls, Carla, into your third bucket of you know, ways people can invest alongside or with. On the first point, I think not necessarily annual. Less frequent would be better. But cost of living increases. I would add that to the definition. We keep the current limits, but periodic inflation adjustments.

MR. FOX: Yeah. I think the one theme I think that comes through -- sorry, are you still going, Greg? Sorry.

MR. YADLEY: No, I'm done.

MR. FOX: Oh. In the comment letters, it was definitely creating -- and the commission is perfectly suited to do this better than us, you know, objective bright line tests. I mean, I think those are working now, and I think that needs to be carried over, perhaps, you know, as we've been talking about on the sophistication side, to the point where percentage of income, percentage of assets does add some subjectivity and more diligence that I think you don't want to have a perverse effect by having something like that. So I think the clear objective standards I think will be best and facilitate and speed up things.

MS. GARRETT: Thank you. Now, how about the assessment -- yes, Phil?

MR. LEVEY: Can I -- can I say one thing, Carla? Sorry. Yeah, I mean, so this is what I found, opinion here, I'm actually -- I think the accredited definitions are fine. Actually, I don't know that we should be looking to create more categories around that. I'm more interested in seeing if there are ways to allow more non-accredited investors into investing vehicles. And so instead of changing the definition of accredited investors, maybe there is a broadening of the exemption where the SEC says if you have more than 50 percent of an investment in a company from accredited investors,

then you can have, you know, the rest of them be non-accredited investors. Because I really think we're looking to -- if I'm thinking about this the right way or we're thinking about this the right way, we should be looking for ways to have non-accredited investors partnering with people that we think are more sophisticated or that meet the sophistication test. And perhaps that gives a better screen, less likely to lose money. And folks are changing -- their position, maybe their changing the access that non-accredited investors could have to small investments, because a certain percentage of sophistication is already involved.

MS. GARRETT: Yeah, Jeff. I think we agree and we think that that is -- we're probably proposing two alternatives right now. Possibly revising the definition of accredited investor, proposing recommendations on that, and also proposing recommendations next with respect to other ways that non-accredited investors can invest in investments.

MR. SOLOMON: Yeah. Maybe one tactical thing to connect the bridges of those two would be expanding the accredited investor definition to include qualified venture capital funds as being an accredited investor. Because then you can -- that's a minor change to the existing structure, which then lets that be a feeder.

Because those can accept investments from non-accredited investors. There would be some others things you'd have to sort of tweak there too from the reporting requirements. But like little changes like that -- I don't know if that's a better pooled investment discussion. But it would be changing the accredited investor definition also.

MS. GARRETT: And that is something that I know we're going to be speaking of. Because we only have a few minutes before lunch, and I do want Youngro to have a little bit of an opportunity to talk about ways that non-accredited investors access the market not through pooled vehicles that we're going to talk about or funds, but through Reg A and Reg CF. Can I just get an idea, are people -- I can put together a recommendation for later this afternoon. Are people generally in support of some sort of broadening of the definition of accredited investor, as long as we look at the other prong too?

MR. GRAHAM: Yes.

MR. FOX: Yeah.

MS. GARRETT: Okay, thank you. Youngro?

MR. LEE: Yeah. And I think some of these topics might come up again this afternoon, so we can talk about it in that context as well. But the main thing that I just want to clarify and put some structure, as you think about this afternoon's discussions is, there is in fact a way for non-accredited investors to invest in private companies, full stop, that is governed by law and much be facilitated through an intermediary. So I think Jeff or somebody might have mentioned, making an assumption again that these things are happening without. No. You have to be a regulated intermediary to be able to facilitate regulation crowdfunding. Full stop. Reg A has to be approved by the SEC in order to be live. So a lot of these fraud situations that unfortunately a lot of people think about is things that are happening outside of the Regulation crowdfunding, Regulation A regime. And that is literally what I was talking about in terms of the intermediaries that are trying to do the right thing actually being penalized in practice because they are trying to comply or trying to do the things.

As a broker dealer, I can tell you from their perspective, we conduct regulation crowdfunding through a broker dealer. We get reviewed by FINRA all the time. We have spent substantial -- a big portion of capital to kind of facilitate this. So that's the one framework that I just would like this committee to completely understand. Regulation crowdfunding, Regulation A, is a

structured offering that is governed by regulation and monitored by FINRA. Full stop. And the reason why I mentioned that is because this directly implies everything we're talking about -- especially Catherine's point about local investment -- I think we're all in agreement with local investments. So as an example of how this applies to accredited investors, even accredited investors, they cannot invest freely in Regulation crowdfunding, which is the vehicle or the legal system to allow local investments, right? So every single investor -- there is no definition of accredited investors and non-accredited investors in Regulation crowdfunding. It's a pure income test. If you make under $100,000 you can invest up to 5 percent of your income. If you make over $100,000, you can invest up to 10 percent. But this means, even if you're an accredited investor worth $100 million, right, you cannot invest more than 10 percent of either the higher of your income or the net worth. So think -- that doesn't make any practical sense.

You can be a retired person with $10 million, and if your annual income is $50,000 you are not -- you are allowed to invest literally nothing in a local restaurant that's raising money or a local brewery that's raising capital. So there's a very fundamental --

in my mind very easy kind of low hanging fruit under the existing Regulation crowdfunding, which there is a $300 million reward for deals completed in that, under that regime. So that's one thing that we don't have time right now, but as we think about the pooled vehicle, just this doesn't make common sense. How do we utilize the existing regulations that have some track record, some data, and apply that in a systematic way to address some of these problems, and just specifically, to even make it more simple. The few solutions might be one, literally increase the amount of capital that businesses can raise using regulation crowdfunding, because it's capped at a million dollars arbitrarily.

Number two is, how can we make the ability to invest under regulation crowdfunding more flexible. And for example that could be not limiting accredited investors to invest in regulation crowdfunding offerings. And two, have a more sensical ability to control that flow. So -- and I think Mike was here, and maybe he can talk about it a little bit. There is literally a precedent -- this is all new. A lot of states, including Texas, had investment limits of $5,000 per investment no matter what. So as long as you can invest $5,000 per investment -- and that's because every business is different -- under the Federal Jobs Act, you

are capped across the entire spectrum of this law. So if you have $5,000, the limit, if you're investing in a crazy flying car idea, and invest $5,000, and there is a multi-million dollar revenue generating brewery that's raising money, you're topped out. You can no longer invest in that deal, because the law has said, sorry, you tapped out on your risky investments for the year. You can't invest in that brewery anymore. So those are some of the structural issues that I want to raise.

And the biggest point being -- I know Sara has tons of experience in it as well -- is that there is a framework that a lot of people over the last six plus years have spent time and effort. And it's startups like us and various other platforms that have spent literally tens of millions of dollars investing and creating a history of this track record, that hopefully would be an easier sell from the committee to advocate for, rather than trying to come up with a brand new structure based on any other considerations.

MS. MOTT: Can I add something to that, Carla? On of the things that Youngro points out very well is that, you know, once -- once they're topped out, they can't invest further. I will tell you, every business is going to need additional funding. There's going to be a need for another round. And again, through your --

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through the crowdfunding vehicle, if you have the opportunity to say hey, look, we need to get -- this company needs to scale but it can't do it without additional capital and it's not bankable yet; can I do another round? And they're capped out. So all the more reason why we need to think about those limits, because they will need capital again.

MS. GARRETT: Thank you. It is now noon, and so it is time to break for lunch. Please note the the webcast will be stopped during lunch, and it will -- the remote participants can rejoin at 1:00. Thank you.

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

MS. GARRETT: Welcome back from lunch. I now call the meeting back to order. I just want to say that we have a lot to get through and this afternoon we have some people that also need to leave a little bit early. So Martha and I are going to work on making sure that the agenda flows smoothly. And so don't take any offense if we try to move people along.

Martha, can you please introduce our next agenda item?

MS. MILLER: Yes, our next agenda item, we have got Rick Fleming, who is the SEC's Investor Advocate, who is here today. Rick is the counterpart to my office and I have loved getting to work with Rick.

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He brings a breadth of experience, having served as the first Investor Advocate and the only Investor Advocate, so he has continued to set the bar high with everything that he is doing. And he comes to this role from having previously been a state securities regulator. And so he has breadth of experience, having seen capital formation and investor protection in the Midwest.

And we thought it would be helpful for Rick to come in and to share a little bit about his office. He also has an investor advisory committee that is similar to this committee in providing strategic advice to the Commission on matters relating to investor protection.

And a little bit about how he thinks about the work that he does from a high level. This is just intended as an introduction so that we can start the relationship with each of you with Rick. And I had a wonderful opportunity to do the same thing with his office.

And for those who don't know, and I think most all of you do, Mark Sharma, who is a member of this committee, serves as the Investor Advocate's delegate to this committee. And he is a wonderful value add from that office.

So with that, Rick, welcome.

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MR. FLEMING: Well, thank you, Martha. Thank you to the members of the committee for the invitation to speak, tell you a little bit about my office and what we do. I also want to thank Mark for sitting in for me and being my delegate to this committee. I certainly am paying attention to the work that you all are doing and am interested in any of the recommendations that you come up with.

A little bit about my background that's, you know, not necessarily part of the bio that normally gets thrown out there. I am a former state regulator. I actually grew up in a little tiny town in Kansas, Leroy Kansas, population 600. So when Catherine talks about the impact of small businesses on communities like that, it really rings true to me. I come from a place where a company with 50 jobs would be a big business, not a small business. And, you know, and I'm still sort of shocked at sort of what we consider a small business at the SEC.

But at any rate, I am really interested in the issues that you all talk about. In fact, when I was a state regulator, you know, everybody thinks of the state regulators of just being in the business of investor protection. But in a small state, especially, and I know Mike Pieciak can attest to this, you know, you

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really are interested in helping the entrepreneur that has some idea that might have this big impact on a small community. So I have spent a lot of time talking certainly to attorneys and doing CLE programs and things like that, trying to help non-securities lawyers understand sort of the ways that they could go about helping their clients raise capital and the different exemptions they could take advantage of.

I actually wrote an article for the Kansas Bar Journal a few years ago, "Helping Small Businesses Raise Capital in Kansas." And in that article, I described a new exemption that we adopted at that time. It was called the Invest Kansas exemption. It was actually the first intrastate crowdfunding exemption. And I actually was the author of that. So kind of a different background than you might expect from somebody that's the SEC's investor advocate. But certainly I've been sort of tuned in to small business concerns for my whole career and continue to be interested in that.

I'll tell you a little bit -- so that's my background. So when I do -- when I do approach issues from the perspective of investors, I try to bring that perspective along with me and not sort of lose sight of the fact of the benefits of these small companies, you know, the way they can impact their communities, the --

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not just the jobs that they bring but how they really impact the entire sort of dynamic of the communities in which they operate.

Anyway, a little bit about my Office of the Investor Advocate. As you can imagine, sort of my primary role is to be a voice for investors within the policymaking context. And so here at the SEC, we review all of the rulemakings that flow through and we take a look at the impact of those proposed rule changes on investors. And I can make recommendations to the Commission about whether I think they're a good idea, a bad idea or, you know, whether they need a new idea, whatever.

And so we -- we have -- even though I'm an SEC employee and I report to the Chairman of the Commission, we really do have sort of an independent role in the Commission, much like Martha and her office. We're supposed to provide that independent voice for investors within the Commission. And I think the idea is basically that, you know, regulated entities interface with the Commission a lot, and so the Staff here at the Commission, the commissioners, tend to hear their concerns and needs a lot. Not so much from your average investor. So we are supposed to be helping to keep those issues, those concerns sort of front of mind for

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the Commission.

We do have, like I say, an independent role. That's sort of underscored by a couple of things. One is again, even though I report to the Chairman, I make my recommendations to the Commission. They are supposed to respond to those recommendations within 60 days. So that sort of is a different dynamic than your average SEC employee. I also report to Congress twice a year and those reports go to Congress without any prior review or approval by anybody outside of my office. So we are, like I say, have that independent role.

I do try to operate mostly more informal than formal, so we don't make a ton of sort of formal recommendations to the Commission. I go around, I talk to each of the commissioners once a month, sort of talk about what's on the rulemaking agenda, what I think about it. And it's relatively rare that we sort of go with a formal recommendation that the Commission is supposed to respond to. So that's sort of the advocacy role of my office.

We also -- a second major part of our office is that we house the SEC's ombudsman. And this is a person that investors can go to if they have some concern or complaint about the SEC itself. So if you're an investor and you want to complain about your

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stockbroker, there is a process you go through to file that complaint. If you've done that and now you're mad at the SEC because we didn't do anything with your complaint, you can come to the ombudsman to try and get a resolution of whatever your issue might be. So you can imagine it's things like, you know, fair fund distributions that take a long time to process and get people their money back, concerns about the -- you know, the arbitration process at FINRA -- sorry -- those types of issues we hear from investors and we try to be as helpful as we can.

A third part of my office is our economic unit. Dr. Brian Scholl, who's actually here, he heads up that part of our office. It has a couple of components to it. One is that we are obligated to consider the impact on investors of proposed changes to rules. So we're either looking at the economic analysis that the Commission is doing and sort of making sure that it appropriately reflects not only the costs and burdens to industry but also the benefits to the investing public. You know, we're reviewing the EA, the economic analysis that the Commission is doing and, from time to time, we're sort of doing our own bit of economic analysis and trying to provide that.

Another part of our economic unit is really

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just research, basic, fundamental research about investors. How do people invest? How do people process information and make decisions with it? Something called decision science. You know, for a disclosure agency like the SEC, all of our -- really, almost all, I guess, of our rules are sort of premised on this idea that you give people information and let them make decisions for themselves with that information. But we know very little about sort of the basic science of how people process information and how they make those decisions. And so we're trying to really elevate the SEC's understanding of things like that so that we can do a better job of providing disclosure that really is decision useful for folks. So we're just getting started with that kind of work. We use tools like surveys and focus groups and one-on-one interviews and things like that that really help us sort of do more to be proactive in terms of getting out and finding out how investors will react to different things, instead of just sort of putting out a rule for comment and hoping that someone actually comments.

The fourth thing that our office does is we support the work of the SEC's Investor Advisory Committee. So much like Martha's office, my office provides the staff-level support for that committee.

I'm actually a member of that committee by statute. So there are a lot of similarities between sort of the construct for Martha's office and mine. In fact, they took a lot of my statute and just replicated it for Martha's office.

But there are some differences. The one main difference that sort of jumps out at me is that one of the questions I get a lot is what's the difference between the Office of the Investor Advocate and the Office of Investor Education and Advocacy, which is another office at the SEC? so There, really the distinction is they're doing all the investor education kind of activity, right? So if the SEC wants to go out and tell people about, you know, different scams or schemes or how to research the background of your broker, that sort of thing, providing educational content to folks, that's a whole other office that does that. My office is really in the policy sphere, trying to provide that voice for investors in the rulemaking process. So that's sort of the distinction that occurs there.

With Martha's office, I gather, she has much more of sort of both of those roles. So she is doing not only the advocacy piece for small business but is, at least for now, doing a lot of sort of educational

stuff about, you know, what does the SEC do and how does that relate to small businesses and, you know, what kind of exemptions are out there, that sort of thing. So there is -- you know, it's not exactly the same role that we perform.

Okay, I thought I might tee up one issue which actually is your discussion this morning on the harmonization concept release. Because this will give you an example of sort of how I interface and sort of how I approach some of these issues.

The harmonization release, I actually filed a comment letter. So I have sort of a wide variety of ways that I can engage in advocacy. And in this case, I did choose to do it in somewhat of a formal method by actually putting a comment letter in the file. But it's not sort of a formal recommendation to the Commission that says, you should do this or you should not do that, you know. So it's sort of this hybrid, I guess.

But in my comment letter, the reason I did it that way is that I actually wanted to try to evoke a little deeper level of analysis from the commenters in terms of how changes to the exemptions might impact investors. I felt like the harmonization release is good. It's especially good in that it does a really good job of laying out all the different exemptions in a

nice little compact summary. And it went through in pretty good detail all the ideas that we've heard from the business community in terms of changes that could be made to some of the offering exemptions.

But I thought it was pretty shallow, frankly, in terms of how it dealt with sort of the investor side of the equation. So it included a couple of things in there that dealt with investors. It basically asked the question of, you know, are investors missing out on golden opportunities by not having access to the private markets? Fair question. It also sort of probed the level of fraud that there may be in the private side of the markets. Again, a fair question, and asked for data on that.

Good questions. But there's such -- there's so much more that we should be asking, I think, in terms of how changes to the exemptions might impact investors or might not impact them. And so I suggested a few other things that I hoped to attract comment about. And those are, you know, just sort of summarized, one would be sort of the investor demand for private offerings. And so, you know, one of the questions I have is, if you change some of the exemptions or the accredited investor definition or something like that with the sort of the premise that that's going to unleash this untapped pool

of capital, is that really going to be true? Or are we just going to wind up, you know, lowering investor protections and not really getting that corresponding benefit of this untapped capital?

And I think that's an important question that we really need to think about. Because if you drill into some of the demographic information that we know, you know, while I wish that the -- that we could change securities laws in some way that would solve economic inequality in the U.S., that is just not a realistic goal. If you look at the demographic data out there, the lowest 25 percent of the population in terms of household wealth, their median financial assets is $1,000. Okay? And that's financial assets, so that's your checking account, your savings account, your investment accounts, anything financial, $1,000. So the bottom quarter of the population, we're not even talking about them. We're not talking about investing in anything, much less private markets.

The next 25 percent, the median amount of financial assets is $10,000. So again, these are households that are just trying to have a rainy-day fund, right? They don't have money to be investing in equities at all, really, much less in the private market. So 50 percent of the population is just sort of gone from the equation. So we're really talking about the upper 50 percent.

Now, if you go to that third quartile from 50 percent to the seventy-fifth percentile of households, their financial assets are more like $60,000. So they do have a little bit of money and they're starting to invest. But generally speaking, they're investing in mutual funds, ETFs, you know, sort of the plain, vanilla stuff that you start to build your retirement. So you get above that and the -- basically, the current accredited investor definition captures like the top 10 percent of households in terms of wealth. And really, there's only a wedge between about that 10 percent and twenty-fifth percentile that has enough wealth that they can sort of sensibly be investing in equities. So there is that wedge of the population. But we need to understand, that's sort of the wedge we're talking about when we talk about opening up the markets, the private markets, to individual investors. It's really just that sliver that is likely to be the candidates for attracting capital from.

And if you drill down on that, you talk about -- well, of those -- of that sliver, seventy-fifth to ninetieth percentile, only one in four of those households invest directly in equities right now. And

that's public equities. So you have to wonder, you know, if there's -- and the median amount is $25,000 that they invest directly in equities and that's the public markets.

So you've got to wonder, if they're investing in public equities at such low rates, even people that have some money, is it really realistic to expect that there's going to be a lot of demand for private investments and startups? So, I mean, it's not that I'm opposed, necessarily, to giving greater access. It's just we need to be, you know -- we need to understand sort of whether there is actually a big, untapped pool of potential capital out there and where that might come from.

The second question I sort of raise is sort of the supply side of the equation. And that is, you know, there are statistics that show, you know, there's a lot of money sloshing around on the private side of the markets, PE funds, VC funds, angel investors. You know, I've talked to PE people that feel like just to, you know, use their capital, to allocate their capital, they're accepting terms that they would have considered just unthinkable not long ago. So there's a lot of money chasing a relatively small number of, you know, really good startups. Now, I'm sure there are some that

are being left out between the coasts.

But I think it is fair to ask yourself, okay, if they can't find PE money, if they can't find VC money and they can't even find an angel group, what quality of investments are we leaving on the table for what would be the retail crowd?

And then finally, I just think we need to think about sort of the challenges that investors would face in the private markets. And so these challenges are -- I mean, they're true for everybody. But they're magnified for a small-dollar investor. So obviously, you've got questions -- you know, you've got issues with liquidity in the private side of the market, you've got informational asymmetries, those types of things. But some of the discussion that you had this morning I think highlights some of these issues. I mean, a person that's participating in the private markets, there is an expectation that they're going to do some due diligence, maybe a couple of days' worth of due diligence. There's an expectation that they're going to be able to bring to bear the ability to value those assets appropriately, to price the risk, as was mentioned this morning. Those are -- those are important sort of skillsets or at least it requires a certain amount of devotion and

determination. And if you're talking about an investor that has maybe $20,000 to $30,000 of assets that they, you know, can appropriately devote to this asset class, does it really make sense for that person to devote two days to due diligence? Or, you know, figuring out the asset valuation, that type of thing. So there are some real challenges, I think.

So it is not just a matter of, oh, investors might be defrauded, or, oh, investors might lose their money. I think there's a real -- there are some real important issues that we need to grapple with in terms of giving small-dollar investors access to the private markets.

Now, I'm going to wind this down because I want to leave time for a couple of questions. But what a lot of this leads me to believe is if the Commission is to go down this road and try to make private markets more accessible to small-dollar investors, the way to do that would be through a fund structure. So I am interested in your discussion this afternoon.

My hesitancy on the fund structure gets to more of a global concern. And that is just the public versus private markets and how the Commission is trying to sort of pursue two really competing objectives. And I think there is a lot of value in the public markets.

We have this rich, robust, highly liquid public market with lots of information. You know, pricing is, presumably, pretty good over there. And then we have the private markets. And we've made it -- we -- the JOBS Act, I think -- I could go into it -- made it basically so it's optional, completely optional whether a company goes public or not.

It used to be, once you got 500 shareholders, you were sort of forced out of the nest of the nest of the private markets into the public markets. And once you became a public reporting company, you might as well do an IPO, might as well list, all of that. Now, it's become virtually optional whether a company ever goes public. And so now we've got a situation where it's costly to be public, it's not very costly to stay private. Why in the world would a company ever go public?

I think we're going to live to regret that one of these days. And I do have a concern that the more that we do to sort of create mechanisms for retail investors to invest in early stage private companies it just sort of contributes to that problem of sort of undermining the public markets because we make the private markets basically a place where you can get all the investors you want, all the money you want, no

restrictions. So why would a company ever go public?

Anyway, with that, I'll leave it for a couple of questions.

MS. MILLER: Thank you very much, Rick. And I appreciate and I love hearing your perspective that we've talked about, that seeing, you know, the SEC has a tripartite mission which is, you know, protecting investors; you know, fair, orderly and efficient markets; and facilitating capital formation. And I think both of us recognize the intertwined nature of that.

MR. FLEMING: Yeah, I think so.

MS. MILLER: So I appreciate you being here today and sharing your perspectives.

Welcome a couple questions

MR. LEE: So thank you for that perspective. And you just mentioned a couple things I wanted to get your opinion on. And there's an assumption in your questioning or explanation that is there a demand, investor demand, for these different companies, number one? And then, is there even good enough startups that are available to supply the investment demand?

So I think those are legitimate questions. But I think the purpose that we're discussing in this committee is that it is literally illegal for the

investors to invest in these types of investments. So if there is no actual way for investors to participate in these what you call perhaps not good businesses, how do you even measure that? Right? How do you begin to measure that?

And I think that's kind of the upside of this committee, is we're trying to figure out is there some acceptable test range, if you will, to plan? But I think that's one of the more -- as an industry person, that's one of the biggest frustrations we get from investors. Because I know, good intentions, like I come from the investment world as well. But the fact that -- and you said that 10 percent -- I think current investors are actually 3 percent of the population. So in that world, if it is literally not possible for individuals to invest in private companies, right, how do you answer your own question?

MR. FLEMING: So, first of all, I challenge the premise. There's a lot I could unpack here. But it is actually legal to invest in a private company. Up to 35 nonaccredited investors can get in a deal. Friends and family rounds have been around forever. And there is, you know, crowdfunding, Reg A, that provide opportunities for the more retail investor to participate in some of these earlier stage companies.

I'm actually a believer in sort of the community-based offering. There are a lot of companies that people would want to invest in, especially in a small community, where you have really mixed motives. It's not just to make a profit for yourself but it's because there's only one pharmacy in that county and if that pharmacy goes down, you're all going to be driving, you know, 60 miles to get your medication. You know, that sort of thing where there is sort of this community appeal and it's local people investing in local businesses.

You know, I think there are good reasons to accommodate that. But I actually think there have been accommodations made for that. The crowdfunding is one example, Reg A.

MR. LEE: Sorry, just to be specific, what I mean is there is not -- existing regulation doesn't provide enough data. I think we all would agree on that, there's not enough data. So that's the point.

When you say family and friends round, there is no such thing as family and friends round. They still have to be accredited investors to participate. So if they're doing it, they're doing it illegally.

So what I'm saying is, is there a way that your office or otherwise thinks there is at least some forum or some exemptions or some flexibility to at least gather the data? Because I think if you ask, I assume, most people on this committee, there is -- the exemptions that you talk about, the '35 rule, nobody uses it. Right? These are not practical ways to gather the data. And that's kind of sometimes the frustration that we get when we're acting with investor advocacy groups.

There has got to be some middle ground for us to at least, you know, just try things a little more. So that was just my general comment on the questions you raise, which are very legit. But I'm -- I'm hoping that there's a middle ground there that we can gather more data on.

MR. FLEMING: Yeah. Like I say, I think -- well, I don't want to debate all this with you. I mean, there is a naked 4A-2 --

MR. LEE: I completely understand what you're saying, too.

MR. FLEMING: Even with crowdfunding, I mean, it's raised some money. But I think the average raise is like $250,000.

MR. LEE: That's correct. Yeah, because it was limited by a million dollars and individuals were limited how much you can invest. And accredited

investors are also limited how much they can invest. So that's what I'm saying. There's a lot of -- I think we're on the same side of the big picture of like trying to improve the capital markets.

But there are systematic issues in the regulation crowdfunding and Reg A. It's not fair to say, hey, you tried this and this works, because there's literally -- the industry, the businesses and investors have their hands tied behind their back. And that's not a fair way to assess, hey, like people don't want to invest in small businesses.

Or I don't know if you were here for Ross Baird's conversation. The person making a million dollars or less, $250,000, they're just not going to be able to get capital from the institutional investors that we are going to hear in a little bit, and so on.

But I personally wish that the SEC investor advocacy group could also take, you know, more practical considerations in place in terms of just gathering data. Right? We don't have to open the floodgates but let's just try to see if we can gather more data by opening a little more flexibility in the existing regimes.

MR. SEATS: I have two questions for you, one easy question, one maybe hard question.

MR. FLEMING: Okay.

MR. SEATS: I thought the quartile, the way you walked through that framing of the investor landscape, awesome, totally loved that. I'm wondering -- I mean, I think we have a shared viewpoint that pooled structures help derisk these private investments in important ways. So that, second, I'm wondering if you think that also could apply to that second quartile? In other words, not just that sliver -- the initial framing sort of felt like a single issue versus pooled, because --

MR. FLEMING: Yeah, yeah. I mean, I'm not thinking in terms of cutting off, you know, strictly you've got to be in the top 50 percent or whatever. Because, I mean, I'm talking -- those are medians, also. So, you know, there are outliers on both, both directions, right? So there are people in that lower quartile that have a little bit of money to invest, or in that second quartile, certainly, there are going to be people that have a little bit of money to invest.

MR. SEATS: I guess my implicit point is that demand for pooled instruments might be greater than demand for single issue because of that sort of dynamic.

And then the harder question --

MR. FLEMING: Probably. I mean, you've seen a shift from investing in individual equities to funds.

MR. SEATS: Yeah, it matches the trend. Right.

So the hard question is, if we can all look at the JOBS Act having an either intended or unintended consequence of decreasing the number of IPOs in public companies, is there an action relative to that 500-shareholder limit before public reporting? Is anyone looking at that as one of the catalysts here to think about?

MR. FLEMING: Not to my knowledge, honestly. I think they should be. But I really think they need to revisit that and see what the impact of that change has been. Because I think that's why you're getting such huge, you know, nonpublic companies, unicorns.

MS. HANKS: At the investor advisory committee last week, there was a lot of discussion about the unknowns in the private markets. We don't know how private investors are doing, we don't know what the return on investment is. Is anyone taking a look at that? Is that something you guys could do? Is it a DERA thing?

MR. FLEMING: Well, it's typically a DERA thing. But in the -- in the request for comment in the concept release, I mean, they basically threw it out to the public, please come to us with data because we just

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don't have it.

You know, one of the criticisms that was raised last week in the investor advisory committee was that the SEC put out a proposal a few years ago that would have actually required some filing of some basic data around private offerings and how much was raised and from how many investors, that sort of thing. And that was never adopted, so we still have just this dearth of information.

MS. MOTT: Rick, there are some things like CB Insights, PitchBook, PwC Money Tree, things like that, that have some data. Have we ever done any studies, you know, extracting data from those aggregators? I mean, it would give us some -- it might not be perfect, but it might give us some indication.

MR. FLEMING: I'm not familiar with those, Catherine, but I would love to know more about that.

MS. MOTT: Oh, gosh, I'll introduce you to them.

MR. FLEMING: And especially Brian. We love data.

MS. MOTT: Those are probably three of them, wouldn't you say?

MS. MEHTA: Yeah, but I think their data is also reliant on what companies issue in their -- if they

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file Form D's, which as we know are not a requirement. It's more of a, you know, we encourage you to file a Form D. And it's after the initial closing, so you don't really know how much they ended up raising and how many shareholders. So I think the data is as good as it can be, but it is lacking.

MS. MOTT: I mean, that was my point, was it's something to start with. It would just be, you know, some indicator.

MR. FLEMING: Thank you.

MR. FOX: Rick, just one clarifying question, just to make sure I understand some of the thoughts that you put out there. I believe I agree with your position on the 500 shareholder and some of the unicorns we have and the issues we have, the need for secondary markets, and this mismatch we have and these big companies, right? But I'm not sure, is the issue of, well, gee, we have more retail investors in private markets, is -- you know, is that, in your mind, is that a singular issue or is that maybe in that particular niche versus, you know, lower down -- I mean, I think Martha gave a very nice analogy at the beginning of the meeting and I don't want to butcher your garage analogy about bikes and --

MS. MILLER: It was terrible to begin with, so feel free to butcher.

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MR. FOX: But essentially that there's a final and, you know, you look at the capital-raising spectrum, you know, there's all sorts of things, right, all the way down from the very beginning companies all the way up to IPOs and even beyond, right? And we've got to look at all parts of the spectrum, right?

And so I think, as we've been thinking about things, you focused on one part of it, right? The unicorns and some of the issues at that part of the capital markets. I want to make sure that we're not losing sight of the fact that we may have companies much earlier in the capital formation that aren't getting the love because we have these mega-funds out there that are focused on unicorns and stuff like that.

Would you -- I just want to make sure that we're not -- you're focused on one issue and it's not kind of polluting through to the rest of the issues.

MR. FLEMING: I mean, it probably is to some extent. Because when you make tweaks to deal with one end of the private markets, you're probably impacting the full spectrum. And I do get less -- I mean, just my personal view, I get a lot less worried about the small startup business in a local community that's attracting investors from the surrounding area that know something about the business, they know the founders, they go to

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church with them, whatever. You know, I have a lot less worry about that than soliciting strangers over the internet, you know, for some large operation, I guess, with little -- with little financial information and that sort of thing.

But it's hard to sort of --

MR. FOX: Regulate all --

MR. FLEMING: -- separate -- yeah, yeah. And one of the issues we've -- I mean, to me, it feels like if an offering is, you know, a few hundred thousand dollars, is that really a federal problem? You know, because I come from an old state regulator background. And I can tell you that I could not shop a $300,000 case to the federal government and get any interest whatsoever.

But I feel like something that's been lost in this is that, you know, the business community and even the small business community has pursued federal regulation and preemption of the states to the extent that, you know, you've sort of got this monolithic regulatory structure at the federal level and less ability to be, you know, I guess, creative, more creative. You know, the states can be far more creative at their regulatory level and, you know, they don't have nearly the difficulty adopting a new exemption.

MR. FOX: Sometimes positively, sometimes negatively --

MR. FLEMING: That's true. That's a fair point, it's a fair point.

MS. GARRETT: Thank you very much, Rick.

MR. FLEMING: Thank you.

MS. GARRETT: We really appreciate your time here.

HARMONIZATION: POOLED INVESTMENT FUNDS

MS GARRETT: And so we are going to move on to our next agenda item, which is what we've been hinting at all day, the pooled investment funds. And so we have some speakers that will be joining us.

So the harmonization concept release included a discussion of whether the SEC should take steps to facilitate capital formation and exempt offerings through pooled investment funds including interval funds and other closed-end funds, and whether retail investors should be allowed greater exposure to growth-stage companies through these pooled investment funds.

To help provide background on various fund-related rules, the committee will hear from two experts today. The first is Richard Horowitz, who is a partner at Dechert LLP. Richard has represented both registered investment companies and private funds for more than 20

years. He has particular experience with alternative strategy mutual funds, such as manager of manager funds and closed-end funds of hedge funds and private equity funds. He is a co-head of Dechert's permanent capital practice and regularly advises alternative asset managers in their effort to assess permanent capital through the business development companies and closed-end funds.

Welcome, Richard.

And we also have with us today John Finley, who is the senior managing director and chief legal officer of Blackstone. Blackstone is an asset management business with over $550 billion of assets under management. Those include investment vehicles focused on private equity, real estate, public debt and equity, growth equity and secondary funds. John is the senior managing director and the firm's chief legal officer and is also a member of the firm's management committee.

Before joining Blackstone in 2010, John was a partner at the law firm of Simpson Thatcher and Bartlett, where he co-headed the global mergers and acquisitions group.

Welcome, John.

These speakers can help provide to the

committee a framework for those of us on the committee who are not as familiar with the legal jargon associated with investment funds and will also answer questions for us.

So, Richard.

MR. HOROWITZ: Thank you. I want to thank the advisory committee for having us here today.

I am Richard Horowitz. I am a partner in the funds group at Dechert. Dechert has the largest registered fund practice in the United States. We represent many of the largest asset managers in the world. I am the co-head of Dechert's permanent capital group, which focuses on closed-end funds and business development companies. More on that shortly.

Over the past several years, I have helped a number of alternative asset managers, both private equity managers and private credit managers, get into the registered fund space, as the private fund world and the registered fund world have been coming together over the past couple of years.

We read with much interest the SEC's May concept release and we submitted our response letter in September, making recommendations on how we believe retail investors can invest in private companies through pooled investment vehicles.

Now, before I discuss our recommendations, I thought it might be helpful to just take a couple of steps back to take several steps forward. I thought it would be helpful to take a minute or two to discuss the three types of pooled investment vehicles that are regulated by the Investment Company Act of 1940.

The first group of vehicles are open-end funds, otherwise known as mutual funds. Mutual funds are the vehicle of choice for the vast majority of retail investors, absolutely. Recent estimates are that over $17 trillion are invested in mutual funds. Mutual funds accept subscriptions on a daily basis and provide daily redemptions. Mutual funds calculate a daily net asset value.

As a result of the daily redemption feature, the SEC requires every mutual fund to invest at least 85 percent of its total assets in liquid securities. A liquid security is a security that can be disposed of within seven days at the price at which the mutual fund is valuing it. Most mutual funds invest, I would say, 95 to 100 percent of their assets in liquid securities. As a result, most mutual funds typically do not invest in private companies; rather, they focus on public equities, public debt, liquid broadly syndicated loans and other liquid assets such as publicly traded REITs.

The second type of vehicle that the '40 Act regulates are closed-end funds. Unlike mutual funds, closed-end funds do not have this 85 percent liquid securities requirement. As a result, closed-end funds can invest up to 100 percent of their total assets in illiquid securities. There's about $250 billion invested in closed-end funds. Compare that to the 17 trillion, right, in mutual funds.

Most closed-end funds are listed on the New York Stock Exchange or Nasdaq and therefore investors trade their shares in the secondary market to each other on a daily basis.

With no redemption feature, listed closed-end funds are a solid vehicle to make private equity and private credit investments in private companies. However, I would say for the most part, closed-end funds have been focusing more on the private credit side of the equation than private equity, and I will get to that in a second.

The listed closed-end fund market has been very choppy over the past 10 years. Many closed-end funds trade at a discount to net asset value. And it has been difficult for underwriters of closed-end funds to raise sufficient IPO proceeds to entice closed-end fund sponsors to move forward with a listed closed-end

fund.

As a result, over the past few years, we and others have been setting up a number of unlisted closed-end funds. These are funds that are offered on a daily or monthly basis. They typically provide quarterly liquidity to retail investors through quarterly issuer tender offers. A growing number of these funds are called interval funds, which mean that they comply with the provisions of the interval fund rule under the Investment Company Act. And we can talk more about that, if you'd like.

The third group again of entities regulated by the '40 Act, business development companies, BDCs. BDCs have been around since 1980. There is about 110 billion invested in BDCs. Again, compare that to the 17 trillion in mutual funds. Under the Investment Company Act, a BDC must invest at least 70 percent of its total assets in what are called eligible portfolio companies, EPCs. An EPC is a U.S. private operating company or a very small U.S. public company, one with a market capitalization of less than $250 million.

The BDC provisions of the Investment Company Act were put in place in 1980 to promote U.S. capital formation for small companies. Thus you might conclude that the BDC is a perfect vehicle for retail investors

to invest in U.S. private companies. Here again, I think the answer is, yes. But BDCs for the most part have focused on the income side, the direct lending side of the business.

We have set up a number of BDCs for clients in the past 10 years. I would say that almost all of them make loans to U.S. private companies, not equity investments. And I think there are two principal reasons for this, and this applies to both the closed-end funds and BDCs. Reason number one, since the financial crisis, U.S. interest rates as we all know have been close to zero. Investors have been desperate for yield. I think I read the other day negative yield sovereign debt is over $12 trillion. It's a little hard to understand.

The private credit investments BDCs make to these small U.S. private operating companies, these are below-investment-grade companies, are high-yielding loans. They typically pay LIBOR plus let's say 5 or 6 percent. BDCs themselves can use leverage. They can themselves borrow money to increase returns, with the resulting dividend to BDC shareholders after fees and expenses in the 7 to 9 percent range. In a zero interest rate environment, BDC dividends of 7 to 9 percent have generated much investor demand, as you

might imagine.

Reason number two, the anti-affiliation provisions of the Investment Company Act make it difficult for many BDCs and closed-end funds to make private equity investments in U.S. private companies. Now, when I discuss the anti-affiliation provisions of the Investment Company Act, I normally like to distribute little bottles of Advil, too, and I apologize not bringing enough for the advisory committee today and I will try and keep it as simple as I can.

The Investment Company Act prohibits a BDC or closed-end fund from engaging in a principal transaction with certain affiliates. And I think that is pretty clear. It also prohibits a BDC or closed-end fund from engaging in a joint transaction, and here's where it gets a little less clear, with certain affiliates. Joint transactions are broadly defined as where a BDC or closed-end fund desires to co-invest with one or more affiliated private funds in the equity of a U.S. private company. That co-investment arguably raises a joint transaction issue for which SEC exemptive relief is required.

Now, the good news is the SEC has granted co-investment exemptive relief to a number of BDCs and closed-end funds and we've obtained that relief for our

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clients. However, that relief is not a panacea. It doesn't cover every possible scenario. And in most cases, a BDC or a closed-end fund sponsor like Blackstone wants to control the U.S. private company it is investing in. That's what private equity is all about. And so in controlling that company, the private equity sponsor will be making a number of decisions about that company, the future of that company, perhaps an M&A transaction, a disposition transaction or a recapitalization transaction, et cetera. All of these subsequent transactions could be viewed as raising joint transaction issues under the Investment Company Act, where a BDC or a closed-end fund is part of the controlling equity group.

Long story short, it is difficult, not impossible, for a BDC or a closed-end fund to participate in controlling equity investments in U.S. private companies. As a result, in our opinion, what we described in our response letter, one of the best ways for retail investors to participate in private companies is through closed-end funds of private equity funds. A closed-end fund of private equity funds is a closed-end fund that invests in 25 to 40 underlying private equity funds managed by the Blackstones, Bain Capitals, Apollos of the world. Each underlying private equity fund

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invests in let's say 15 to 20 portfolio companies. Thus, indirectly, through the closed-end fund, retail investors would have investment exposure to 300 to 500 portfolio companies.

As we have discussed in our letter, the SEC up until now has prohibited retail investors from investing in closed-end funds of private equity funds, taking the position that these funds are not, quote, unquote, suitable for retail investors. And they imposed an accredited investor standard for eligibility to invest in a closed-end fund of private equity funds.

Two important points here. It is unclear to me where this position came from. It is not based on the provisions of the Investment Company Act and it is not based on the provisions of the Securities Act. I don't believe it is the job of the SEC to decide which investment products are, quote, unquote, suitable for retail investors. I believe it is the job of the SEC to ensure that the disclosure about an investment product is accurate, clear and complete, and that retail investors have the relevant information they need along with their investment advisor or financial advisor to evaluate the risks and rewards of the potential investment product.

Institutional investors and accredited

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investors have been investing in closed-end funds of private equity funds for many years. We are currently setting up three new closed-end funds of private equity funds for clients. The demand for these funds is there.

I believe the time has come to permit retail investors to invest in closed-end funds of private equity funds and other closed-end funds of private funds. This would include, potentially, a New York Stock Exchange listed closed-end fund of private funds, as well as unlisted closed-end funds of private funds. The key point here is that making this change would not require any amendment to the Investment Company Act, it would not require an amendment to the Securities Act, it would not require the SEC to adopt a new rule under the Investment Company Act or the Securities Act. It would simply require a change in the SEC's informal position that these types of funds are not appropriate or suitable for retail investors.

Closed-end funds and BDCs have proven to be excellent vehicles for retail investors to participate in the private credit investments that they make. In my opinion, closed-end funds of private equity funds are an excellent vehicle for retail investors to participate in private equity investments in private companies. And we

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recommend that the SEC change its informal position and permit retail investors to invest in these types of funds.

Happy to take any questions.

MS. GARRETT: Can we hear from John first?

MR. HORWITZ: Sure.

MS. GARRETT: Thank you.

MR. FINLEY: As Carla said, I'm John Finley. I am the chief legal officer of Blackstone. And I am very pleased to be with you today and talk about alternatives, the opportunity of alternatives for the retail area. And I was also interested to hear the comments of Rick Fleming because we really are very much in agreement that this is an opportunity but it's also a risk that needs to be managed really well. It is not in the investors' interest, it is not in our firm's interest and it's not in the industry's interest to have a product be flooded into the market that is not a good product that investors don't see good returns on. That would really be extremely regrettable. And therefore, we agree, we need to be really careful how this gets looked at and how it gets into the marketplace. But it does come back to there is a great opportunity here.

So just to -- I did some slides and I'll try to get through them -- there we go.

(Slide.)

MR. FINLEY: So this slide basically shows what the point all is about. And this was done by the Committee on Capital Markets Regulation, Voya, showing returns on PE performance verses the S&P. It's not the only way of looking at it; others look at it differently. But this is the case that the PE return beats the S&P over time. Because if you sort of cherry pick periods either one way or the other you can get different results.

And I'd say what's also really interesting about this is the volatility of private equity. And I'm talking about private equity, but I really mean private markets. You know, it could be real estate, whatever. And private equity, while we may be best known on the bigger side of the deals, also includes venture which we're not part of, growth we're getting into which is sort of the stage between, as you know, venture and private equity. So it really applies to all. So in terms of these returns, the thing that's really interesting is the volatility is actually lower in the private markets. And it's really for two reasons.

First of all, a private market, you value based on a DCF. So of course it's not going to bounce around like a public market. And second of all, in a

private, you have the ability to intervene very quickly and anticipate and act in ways that you can't in the public markets. And both those things dampen volatility. So there are plenty of studies that will show that, with alternatives, not only can you get higher returns but you can reduce volatility.

(Slide.)

MR. FINLEY: Moving along, this basically is just showing that private capital, median net RRs, and this shows private equity, private debt, real estate, infrastructure, pretty much on average exceeded 10 percent. So that's pretty self-explanatory.

So again, you know, the why now? I won't dwell on this too much because you're all probably pretty familiar why now. And that is that the private markets have never been more robust. And that means that companies come to market at a later stage, the opportunity is not as great as it was, and the number of public companies is declining precipitously. And at the same time, we see that retail investors are under-allocated to alternative asset classes. So this will -- I'll go back one.

(Slide.)

MR. FINLEY: This was basically again sort of a restatement of where we were. Again, you're probably

pretty familiar with where Jay was on this, the retail investors have less access to the market. That is for sure. Whether we want to expand that goes to again how do we manage the risk through that.

You will see from this chart in the lower left that the number of startups has just exploded in terms of again the expansion of the private market. So we've again come to the issue of it's a really large market to have people excluded from. To the point, the data isn't great in terms of an industry basis, this private market, how much of this demand is out there. Certainly, we're seeing, as we expand our retail efforts, anecdotally, you know, we're seeing a lot of expansion. There are stats that I saw that were older that shows that the mass affluent, which is basically 100,000 to a million, is expanding quite dramatically. It was about a half a trillion in 2004. By 2015, according to Pricewaterhouse, estimated at 2.8, forecasted later again to go higher.

We also find from our own investments this demand. We have a product called a BREIT, which is basically a non-listed REIT. It makes commercial real estate available. But it's more income oriented than opportunistic. And it has minimum thresholds but they're lower, much lower than accredited. So it's the

NASAA, and so it's a 250K and then 70 or some combination. And we've raised relatively quickly on an unlevered basis 10 billion and 24 billion on a levered. And there is just tremendous demand for the product.

So we are seeing a lot of product, whether it's for -- a lot of perpetual vehicles out there. And we're certainly getting, as we expand through independent broker-dealers or registered investment advisers, both those firms, we're hearing demand for these alternative products. And it's not a surprise why. Look where interest rates are and look at where returns are. Yes, stock market has been up 23 percent this year. But overall, people are looking for, whether on the credit side or otherwise, a greater return. So we are seeing that demand.

(Slide.)

MR. FINLEY: Next is showing again, you know, again, the decline in the public -- the public companies. There is no real surprise on that. Coming later to markets, as I mentioned.

(Slide.)

MR. FINLEY: And if you look at the next page and you look at the average allocation to alternatives, so pensions 27 percent, endowments 29 percent, and individual investors less than 5 percent. So if you're a registered investment adviser, you're an independent broker-dealer, you're looking out for your client, you're saying, gee, what should this allocation be? That's really where a big driver is.

That even if you say, we don't want the same allocation to a pension or endowment, I won't even get into that, but is the percentage right and do we really need that to be higher? And that's also a reason why we both see an opportunity and both why we believe we're seeing a lot of demand is that underallocation.

(Slide.)

MR. FINLEY: It's not just we that see it. And before I get to this, you know, I was very interested to read the ILPA letter that came in, the Institutional Limited Partners Association, which is an institutional view on the perspective and certainly not a captive of private equity. And they strongly believe in the benefit to investors of investing in the private markets. And they continue to believe in this allocation to private equity because there are yields that just cannot be attained in the public markets.

And so that really is the essence of the question. What's good enough for these institutions? Is there a way to get the public markets -- is there a way to get retail investors to get exactly what the

institutions are saying they want? And that comes back to Rick. Which is, can it be done in a way that's managed very safely? Institutions are not retail investors, so the way that gets done is going to be different. But it goes to the opportunity.

(Slide.)

MR. FINLEY: And over a period of years, this is just showing that the growth of the $10,000 investment over a 30-year period, just how dramatic the difference is when you have that increase over the S&P. So I won't dwell on that. But it is a pretty interesting stat of just how dramatic it is over a period of years, as someone is sort of looking for their retirement or investing for their retirement.

This slide didn't come up; I don't know exactly why.

But basically, what this is -- what you would have seen if this were up there is what we're doing to address some of the issues as we go out to the marketplace to manage some of the risk. So we are doing a tremendous amount of education to the registered investment advisers and the independent broker-dealers. We are tailoring products specifically to the retail market that's designed for their needs. We are investing in proprietary systems that allow us to track

the investment data very, very carefully, rate investments. And we are working through increasing employees and dedicated service platforms, all which make us more effective in addressing that market.

We certainly, in terms of the demand, you know, the private wealth, AUM raised, has gone from in 2011 220 million to 25 billion now. So that again is showing -- now, of course, some of that is accredited investors, whatever. But if you're looking at mass affluent and you're looking at high net worth, tremendous amount of interest in these products.

(Slide.)

MR. FINLEY: Also that's -- I didn't realize it went there. So there you have it. It gives all the things that came in. It is more sophisticated than I was ready for.

So what are we thinking about? Well, the way we have been thinking about it and we didn't put it in our own letter but the AIC did, the American Investment Council and generally supportive of their views, is really -- and again, the ILPA is instructive because again, it's not an industry player, it's rather a customer.

ILPA said that, rather than direct investment, they think investing through a registered fund vehicle

would be preferable for most retail investors and the Commission should consider this model. And that's really what many of -- what these proposed regulatory changes are focused on. Because rather than looking for the investor to sort of have to pick out the next Uber or avoid WeWork, whichever way you look at it, through the pooled vehicle, you get not only diversification, but you get all the advantages of an intermediary to providing.

And one which Richard mentioned right off the bat, this eliminating the accredited investor threshold for offering of registering of funds of private funds. This is probably the most obvious way to address the issue, which is that the Staff requires that offerings of registered closed-end funds that invest more than 15 percent in private funds be limited to accredited investors. And a number of commentators have encouraged the SEC Staff to change that policy because that basically would allow you then to have a registered closed-end fund that would have a substantial investment in private funds, could be diversified, you'd have the intermediary and you don't have the risk of the demand, you know, everybody looking for their money because it's a closed-end fund, of course. You all know this.

So this provides one route. Others, not

getting in the weeds too much, easing the liquidity restraints for target date funds. Target date funds are terrific vehicles for long-term investing. And when you're young, obviously, again, you guys know, invest in something that's locked up for a while and then gets more liquid as you get older. And this would facilitate being able to be in illiquid assets. And finally, more carry-like compensation for retail funds.

But also in terms of managing the risk, the risk
-- you know, the framework of going through a regulated pooled fund is, of course, one way of managing that risk, managing that issue of the individual investor. But we also saw commentators who focused on access to experienced managers, either having managers that meet scale and experience, not people that are learning on the job first time in, and also having retail be no more than a percentage or having the retail be invested with a manager who has a tremendous institutional following.

I mean, that will do two things. Number one, they can draft off of the institutional terms and conditions. And also, if an institutional investor is invested substantially, that gives one a level of comfort that might not be the case if a manager only has retail money. So that would be -- the suggestion is

that the SEC should consider limiting retail access to managers with an institutional investor base. And that certainly would provide another layer of protection.

So you've got the pooled vehicle, pooled vehicles that are managed by managers who manage institutional money and then opening that up more to retail.

So with that, I think Richard or I would be happy to answer any questions or go into more depths on these topics.

MR. YADLEY: Thank you both. You made very complex information understandable.

Earlier this morning when we were talking about this subject, one of the things that came out is part of the scale that has been created quite successfully with funds such as Blackstone is investing in larger companies, later companies, you have a lot of money to put to work. And a lot of the smaller companies need smaller amounts of money.

Would you envision that funds would be created with these rule changes that would invest smaller amounts of money in earlier stage and developing companies?

MR. FINLEY: My focus has been what I know best. And so the focus has been on the larger scale

funds. But I see no reason that the principles wouldn't apply. We -- Blackstone is not only at the biggest size investments because we have a tactical opportunities fund which is opportunistic and has no minimum, makes actually quite small investments. And we also have a growth fund, which I mentioned, which is between venture.

Now, we don't go to the smallest venture. But I don't see any reason why venture can't be subject to the same principles, as long as the same protections are in place. And certainly the diversification in a pooled is ideal when dealing with venture.

MR. HOROWITZ: My answer, similar. You know, there are a number of private equity managers that I've never heard of that are doing really good work investing in smaller companies. And smart fund of funds managers are out there looking for those managers, those private equity managers, wanting to put their funds in a pooled investment vehicle. So I think the answer is yes, you would see -- it's one way that a fund of funds manager can distinguish itself from sort of the larger, more traditional -- the larger, you know, buyout fund managers, is to find these smaller managers. Managers, I should say, that focus on smaller companies. I do think you would have a mixture of closed-end funds of

private equity funds, some larger, some smaller.

MR. SEATS: Gentlemen, thank you for all the information. I agree it was a great walkthrough.

So what -- the commonality between both of your framing and I think many of the comment letters I think has a lot of alignment in this room, which is that the way to address some of these risks is to pool investments into portfolios and that you are addressing some of the primary concerns there. And then to figure out how do you get alignment with fiduciaries in the middle.

I think both of your suggestions were down the line of having a fund of funds approach, you know, registered fund of private funds. And in one -- and it has the nice feature of saying, hey, this already meets the regulations but it doesn't meet the Staff sort of policy position, so it's an easier -- maybe an easier attack surface.

But the thought I have on this is, is there a risk of sort of the extra layers of fees in the middle of those structures? And are you choosing that path because of expediency or -- I mean, in other words, can you achieve the same net effect with a larger pooled vehicle that has the same underlying investments versus having multiple layers? And maybe another way of asking that is if you need to enter a position of fiduciaries as part of the sort of selling point on it.

MR. HOROWITZ: It's a good question. I'll give you my answer. You know, I would say that a fund of funds manager is providing a high-quality service in evaluating the thousands of underlying managers that are out there, having this complex database of performance, right, that they've accumulated. And so to pay the -- yes, there are two layers of fees, right. There's a management fee at the closed-end fund level and then a management fee and a performance fee at the underlying private equity fund level.

And I would say net of all of those fees, it is -- you are getting -- an individual investor is getting a diversified portfolio, a noncorrelated portfolio of exposure, right, away from the public equity markets that is important, I would say, for his diversification, her diversification.

So I think -- I don't have the statistics on the overall performance after fees but I think it's been solid. I think fund of funds performance has been solid over a long period of time.

MR. FINLEY: Yeah, I -- this is a great question. I would have liked the question to be asked without even knowing you were going to ask it. Because

a couple answers on it.

One, interestingly, if you do do a fund of funds, you can't have an affiliate of the fund --

MR. SEATS: Richard asked for exemptive relief on --

MR. FINLEY: Right, but if you did -- but the point is, to your point about fees, you might be able to get much lower fees if you had, for example, a Blackstone group of funds, real estate and credit and PE, and then manage that through, be able to do it much more -- at a lower cost than is done today. So that's one answer on the fees. Fees, you know, certainly have to be managed.

The other is, some of the issues don't relate just really to the fund of funds, like a target date fund. You know, giving more flexibility to just have a manager say, you know, I want to put a private equity fund into this that's being managed otherwise, that also is necessarily going to create a fee issue, it's going to not make it work on a net basis.

So it's a very legitimate issue. The fee issue and the net and where you are on a net basis is, you know, critical. But I do believe one way or another, they can be managed through based on just two examples, two I just went through.

MR. SEATS: The underlying performance data that you showed, is that levered or unlevered on the PE numbers?

MR. FINLEY: Levered. But, you know, PE -- the PE, it used to be that leverage was the biggest driver of PE gains. And as some of you may know, that's really not the case anymore. Operating improvements is really a much bigger factor in leverage. And nonetheless, the volatility returns also reflect leverage.

And little known, but if you take private equity investments of similar quality to similar credit of non-private equity, the bankruptcy rate is actually lower on private equity than non-private equity for the same level of credit quality.

MR. SOLOMON: Could I ask -- hi, Richard. Sorry I missed you on the train this morning.

MR. HOROWITZ: Oh, Jeff Solomon. How are you? By voice, calling in.

MR. SOLOMON: Yeah, can you guys just walk through what would the mark to market regime be on these products? Because so much of the challenge associated with BDC marks, and ultimately how NAVs get reported to individual investors, you know, people take a look at Level 1 assets and that's really, you know, at the end

of the day how -- especially if you're dealing with several funds in this framework, how would the mark work and how would you suggest that the investor should get comfortable with that regime?

And then a follow-up question is, if you are - - well, actually answer that question first and I'll follow up.

MR. HOROWITZ: So in a closed-end fund of private equity funds, you've got illiquid private equity fund investments, right, that the closed-end fund has made. Those are Level 3 assets, right? The manager of the closed-end fund is getting reporting, right, from the underlying managers on a quarterly basis of how that manager is valuing its portfolio companies. In between quarters, that manager provides other information, I guess I would say, about the portfolio. Meaning it's calling capital, it's disposing -- it's doing dispositions of portfolio companies. There is information that's provided in between the quarters as well to the closed-end fund manager.

You know, a closed-end fund, as I said, under the '40 Act, has to have its own valuation policies. There's a board of directors of the closed-end fund, a majority of whom are independent of the adviser. That's a '40 Act requirement. The board has a role to play in approving the valuations, right, for the closed-end fund.

And so I guess I would say it's certainly difficult, right, for the closed-end fund manager to have better information than the underlying managers about those portfolio companies. But the closed-end fund of funds managers that we work with have very sophisticated valuation models, very sophisticated databases. They are monitoring these funds and the portfolio companies in these funds. And I think if I'm a retail investor, I can take a lot of comfort in all the work that's being done by the fund of funds manager in coming up with valuations for that closed-end fund.

MR. SOLOMON: So my follow-up question is if you're dealing with publicly traded or publicly listed BDCs and they fall below the net asset value, would you be proposing that there be a -- of how they can raise -- capital? Because I think that's always sort of, I think, the -- for publicly traded BDCs. And if you had mostly private equity oriented -- you know, how would -- how would that -- you know, how do you think that might work?

MR. HOROWITZ: That's a good question.

So what Jeff is asking about, there are a number of BDCs, right, that are listed on the New York

Stock Exchange. There's a '40 Act provision which says if your share price is trading at below the then-calculated net asset value, you cannot issue more shares in that discount situation. And that provision in the '40 Act is meant to prevent dilution to the existing shareholders.

You can go -- under the '40 Act, you can go to your shareholders and actually have a proxy and ask them to approve a proposal to allow the BDC or closed-end fund to issue shares at below net asset value and many BDCs have done that from time to time in an effort to say to the investors, you know, we want to have some cash, we think there are good investment opportunities here, we don't really -- you know, we're not bothered by the fact that our stock price is trading below our calculated net asset value. We want you to approve this proposal. That proposal, if approved, would be good for one year.

I would say a closed-end fund of private equity funds would probably operate in a similar manner. You know, how would the stock price trade? I think that's the question you're asking, right? It's a good question, it's a very good question. You know, part of the answer to that question depends on how much information, right, can be put out there on a regular

basis in terms of what the NAV of that closed-end fund is to try and ensure, give comfort to the marketplace that, you know, the underlying portfolio companies are performing as we expected and so on.

But I certainly, you know, wouldn't be surprised if the closed-end fund's stock price from time to time trades at a discount to NAV.

MR. FINLEY: Yeah. I'd also -- you already have alternatives that have the issue of valuation and mark to mark. I mean, you've got alternative multistrategy funds that have hedge -- you know, multiple hedge fund managers that the central manager has to get valuations. You have BDCs and credit for alternatives where there's valuation issues of all the alternative assets and, you know, investments in a variety of companies. And some, you even have nonaffiliated managers with some private equity that are being done, whether here or abroad.

So it's a great question. But again, if there were a will to sort of say we want to do this for the investor, that kind of mechanic can be worked through.

MR. SOLOMON: I think you guys did a great job of making a very complicated area, topic very understandable, so thank you.

MR. LEE: My question was -- thank you for,

again, making this -- I think we're all in agreement, generally, in the gist of what you were saying. But I think part of this committee mission and the SEC in harmonization also was not just about opening access to retail investors but actually from the business perspective of bringing capital to the local businesses, local economies that, I'm generalizing a bit, but the big firms you mentioned generally are not investing in, let's just say, a local investment that was presented earlier, which was a small food product company in Kentucky, for example.

So one of the things that, while I complete -- agree -- and with Rick as well, on the investor protection sense, of like let -- let investors, retail investors, invest alongside managers, quote, unquote, with scale and experience, the problem, if you will, as a matter of practice, that there is no institutional investor with scale and experience that has focused on investing in these local, smaller investments, right? Because of the systematic matter.

So I'm just -- obviously, there is no right answer. But I just wanted to get your thoughts on, from your perspective, as leaders of the investment industry, how could you utilize these laws to bring capital specifically to smaller businesses? I'm not talking about the $50 million small business; I'm talking about the 500,000 revenue small businesses. Because I think that's, if as big, if not biggest -- or at least to some members of the committee, that's what the passion is, to try to bring capital to those businesses.

MR. FINLEY: So if what you're saying is that the way in which either venture or growth funds, as they're operating private equity funds of which there are thousands, that even with those with experience, they're just not going to be making at any of those levels those kinds of investments for the firms that you're addressing, while I wasn't prepared to address that because I thought at some of the ranges, that would be still viewed as small business capital formation. But I would say that I would err, at least from our perspective, on having firms with scale and experience as we move into an area that's new. And we can see how that goes, maybe.

But given that we've got all these -- we don't have all these, but the three intertwined objectives, yes, capital formation. But we have to do it in a way that's managed safely for investors. I would have some concerns on that, in terms of what I would call opening the gates and having retail investors have managers without scale and experience.

Personally, not only am I concerned for the investor, but I think it's terrible for the industry if there is a -- the wrong players get in. We've seen in certain areas where wrong players do get in and the industry really gets tainted and nobody wants to get in, and in the long run it actually hurts capital formation when there isn't the credibility. So I would be very cautious with that.

It may not be exactly what you're looking to hear. But that was my perspective on that.

MR. LEE: That's actually a very legitimate perspective as well. And I guess this is an open question. It really is the fact -- I think that was the point, right? Because of that assumption, which probably is valid, statistically. But the reality is there are a lot of businesses in these small markets that require capital. And the flipside is there are individuals that are not accredited investors that, because of their local -- locality, relationship, reputation, want to invest in these businesses. And so, yeah, maybe the answer is under this exemption, that's not the right -- there's some other way to do that.

MR. FINLEY: Exactly. It may not be this particular pooled vehicle.

MR. LEE: But I think this -- this is a good

as a highlighting, an unintended consequence of limiting it purely to an experienced -- scaled and experienced manager might be again the persistent problem of capital to local businesses, especially women, minority, immigrant founders. Which is a huge proportion of companies that are utilizing regulation crowdfunding for specifically that reason.

So that's just one thing to highlight to the overall committee, is this is very good but there are other issues.

MR. HOROWITZ: I would add one thing. BDCs, we've set up a number of BDCs for clients. Typically, the BDC is making a loan to a company with, you know, EBITDA of let's say 5 million to 100 million. So you're right in saying even a $5 million company is not sort of the company -- in earnings is not the company that you're sort of focusing on, very small companies. But that BDCs do go down, I would say, to that level to make loans to companies like that.

We did set up a closed-end fund a couple of years ago for a client which buys consumer loans from SoFi and Lending Tree and pools, buys thousands of them, right? And it's a fund that now has about 500 million in assets, so it's gaining in popularity. And so I would note, I think, that there is maybe some potential

to pool very small loans from these kinds of marketplace lenders, right, and put them in a registered fund. And the schedule of investments for that fund goes on for many pages because they literally have thousands and thousands of small loans on their balance sheet.

MR. SEATS: A question related to that. The -- how do you think about the tension of the disclosure requirements? So in that example, these are private companies, but their loan principal is in a public disclosure list. And maybe in that fund of -- registered fund of funds structure, you've got one layer of shielding on that.

But do you -- how do you think about the tension of some of the benefits of being a private company connected to the public disclosure requirements of retail capital?

MR. HOROWITZ: Yeah, I do think that that is a benefit of a closed-end fund of private equity funds or a closed-end fund of private credit funds, in that the investments that are presented are the underlying funds that the fund is invested in, right? You don't look through to the portfolio companies in those funds for SEC reporting purposes.

And, you know, if that's important to those portfolio companies, they have that level of, you know -

- the confidentiality, whatever, is still there.

MS. MOTT: I was going to ask about concentration of PE in major cities. We see in VC 80 percent of it is in three cities. But 55 percent of the angel capital is in the middle market, and 45 percent in those three major cities.

How do you see that in your own -- in your PE world, if we encourage that -- so we now allow retail investors to participate? Will you get too much money maybe chasing the same deals? Would you drive down the returns? I mean, you know, when we think about this, how it's going to maybe impact the market?

MR. FINLEY: That's a legitimate issue, which is
-- and ILPA raised that issue, too, which is that one needs to be cautious. And they're concerned because they're saying, gee, if all this retail money comes in, are we going to drive down the returns? And therefore, that's why -- the way we look at it. On the one hand, we see that there should be some democratization of these opportunities and it's good for the investors and it's good for our industry if this is a product that's more widely available. But we have to do it in a very measured, cautious way that gives investors the opportunity for really the investors with scale and

experience and institutional base. But that's part of the balancing in how much you open up.

MS. MOTT: So could you -- I'm sorry.

MR. HOROWITZ: I was just going to add one quick thing. When I look at the portfolio companies, let's say, our BDC clients have invested in, they made loans to these companies. These companies are throughout the United States, which is very interesting. BDC, as I said, has to invest at least 70 percent of its assets in the United States, so it is a U.S.-focused vehicle. But they have that 30 percent other basket and often are making loans to non-U.S. companies. And you are seeing very interesting companies outside the United States that they are loaning money to.

I would think you would see a similar kind of distribution if you looked at those 300 to 500 portfolio companies, right, in my example in a closed-end fund of private equity funds. My guess would be you would be seeing very interesting companies in lots of different industries across the United States.

MS. MOTT: So could there be an opportunity for sector funds, so to speak, that focus on regions or specific regions? So could this model work in something like that? And let's say, when we say sector funds, like maybe manufacturing and then another one in

logistics or a balance of some percentage of manufacturing, a percentage of logistics, a percentage of robotics. You know what I mean? Something like that, that focuses on an underserved area or something like that?

MR. FINLEY: That's the way PE has really developed. So as PE started in our firm with global opportunistic funds, it then went towards either regions or industries, whether it was energy. Some of the firms specialize more, even in PE, within tech. And so that will be a natural evolution as you get bigger and bigger scale and the industry is much bigger and people are expecting to allocate more to it, if you look at -- industry source and they ask managers, are you going to allocate more to private equity? The answer is, yes. And as that happens more and more, and to your point about chasing, you start to go more niche. And that will only be a continued evolution.

So when you think about private equity, you really have to say, gee, Asia fund, European fund, European real estate fund, energy fund, you know, it really gets sliced up a lot for the benefit of the investor.

MR. HOROWITZ: We're in the process of setting up a new closed-end fund. It's going to focus on

distressed investment opportunities. I think that's interesting, right? Everybody is sort of waiting, right, for the shoe to drop. And, you know, it's a well-known manager. You know, lots of people around this table have heard of them and they have an excellent distressed reputation, right? And so retail investors will be able to invest in that fund. I think that's interesting.

MR. TORBERT: John, Richard, can I ask you a quick question? Because we're really focused on making sure that some of these smaller regions and companies get financing. So can you help me understand?

Traditionally, what happens is, as the funds get bigger, quite frankly, they keep looking for bigger and bigger deals. What incentives can we put in place that, if we allow more retail investors to put money into your funds and others, that you then begin to focus on the manufacturing effort or manufacturing fund in West Virginia or whatever region? How do I know that you guys will continue to stay in focus on those types of reasons? Or will you just go upstream like we normally see happening every single time something changes in the market in favor

MR. FINLEY: But again, it may not be satisfactory because the larger firms do have minimum threshold investments and they're high.

MR. TORBERT: Of course.

MR. FINLEY: But you do have thousands of private equity firms. And I think you could speak to it more in terms of middle market or smaller, that when the opportunity is there for returns in a neglected market, the opposite -- these big deals are flipside. The bigger firms, with the competition, they're, you know, the only ones who can do the big deals so there's less competition.

But you do have areas in the market, much smaller deals that firms that aren't here and you haven't heard of, that are focused on those smaller deals and they have experience and they have a good track record.

Maybe hear from Richard in terms of the size of the kinds of deals you're seeing with your middle market practice.

MR. HOROWITZ: Yeah. No. Right. So Dechert has a large private equity middle market practice, right? We represent private equity managers that do buyouts, you know, in the hundred million to 500 million range, not necessarily billions of dollars. Those are small companies. They're not micro companies, right, but they are small companies. And they are companies

that could benefit tremendously from the expertise that these managers, right, can bring to the table to help them grow and so on.

We see a number of managers focusing on the middle market, I would say small to middle market companies, because there are more opportunities there for returns. I agree with you. Right? And I think the returns will dictate where these high-quality managers look in terms of industries and sectors and all that good stuff.

MR. TORBERT: Can I ask you one other question? Which is, are there any other incentives that the SEC can put in place that make companies like, say, the Riverside Company or GTCR or some of those folks that you and I know, are there incentives that we possibly can put in place that encourage them to go downstream, mid and then downstream, so to speak, structurally?

MR. FINLEY: That's a good question. You know, I tend to look at the SEC as more of a disclosure and protection regime. And so it may -- I mean, certainly it should be looked at. But it may be that that's got to come from other areas in combination with giving that flexibility and that it can't really be by the SEC alone to address that issue.

MR. HOROWITZ: I could probably give the same answer, right. Tax benefits seem like something that is outside certainly the SEC's, you know, bailiwick. But it seems like to encourage investment flow into areas that need to grow and need to benefit from inflows, capital inflows, yes. Tax benefits, yes.

MR. TORBERT: Thank you, gentlemen.

MS. GARRETT: Thank you very much, John and Richard. We really appreciate all your insights today.

MR. HOROWITZ: Thank you for having us.

MR. FINLEY: Thank you. Enjoyed it very much.

MS. GARRETT: As people said, you made very complex issues simple for those of us. Thank you.

DISCUSSION

MS. GARRETT: And for the committee members, now that we have had all of our speakers for the day, we can continue our deliberations and discussion on harmonization and any recommendations.

You know, I might say we might want to start with what we've just heard about the pooled investment funds and what people's thoughts are in terms of developing recommendations for this committee to vote on today.

MS. MEHTA: I would be interested in hearing, since it's not really part of the rules but just the way

the SEC has enforced that 15 percent rule of not more than 15 percent can go into illiquid assets, can any of you speak any more to why it has been that way and what -- what you are trying to protect and do you think that's working? Or is that really up for debate, to get rid of that 15 percent threshold?

MS. MILLER: Eyes are on me. And so I am going to go right outside of my lane and so I'm going to keep it -- earlier, Ross said he was at the 10,000 or 100,000, so we're going to go to million-foot level.

But when they were talking earlier about redemption, it goes to the liquidity requirements with those funds. And so that's a threshold that's been set for that. So closed-end funds provide just different flexibility, given the differences in liquidity requirements there and the lack of redemption -- daily redemption requirements that mutual funds have. Which is why you have two very different types of funds; they have very different types of investments they can hold because they have very different ways that they interact with the shareholders and investors in those funds.

Does that answer it in two sentences? Please don't make me say another one --

(Laughter.)

MR. SEATS: I mean, to support that point though, the reality is they could have 15 percent in illiquid. But the industry is 5 to zero percent in illiquid. So not even approaching the 15 percent mark, out of caution on ability to create -- you know, to satisfy redemption. So it sort of points to mutual fund constructs, not the right formulation.

I think the question -- the question I'm interested in was similar framing but different like predicate is that the policy position that doesn't actually match the regulations on accredited investors having access to invest in -- nonaccredited investors in registered funds of private funds. Like that was the one thing -- that was the point they were hitting on, is this is not -- this is in line with '40 Act, this is in line with all current regulations. This is sort of a Staff position.

So I don't know if that -- did that resonate? Is there -- I don't know if there's more -- if there's something to talk about on that one.

MS. MILLER: I think it's up for debate.

MR. SEATS: Yeah.

MS. GARRETT: Just to be clear, is there a Staff position right now that nonaccredited investors can't invest in registered closed-end funds that invest more than 15 percent of their assets in private funds?

Is that the current --

MS. MILLER: There is guidance on that, yes.

MS. GARRETT: There's guidance on that right now. Okay.

MR. LEE: And also Regulation Crowdfunding specifically prohibits raising -- using Regulation Crowdfunding for purpose of investing in funds. So that's a statutory limitation.

MR. SEATS: I mean, I could throw out there that -- I mean, we could debate the scope of this committee and how much like changing that guidance actually affects small business capital formation. But all of that aside, I think the argument is an extremely logical argument in terms of democratizing access for investors into that particular asset. So I -- you know, it resonates with me, I guess would --

MR. LEVEY: Yeah, it sort of -- it's one of the two prongs of what we've been talking about. And I think it resonates with me, too, and it would have all the protections that are there and that were referenced. And I would be in favor of opening up to Main Street investors, nonaccredited investors, that. But then I think we ought to talk about the access to capital prong.

MS. GARRETT: I was just going to summarize. I mean, if we want to then talk about also the other ways that smaller companies can raise money other than through these large, pooled investments, it sounds to me like there may be a recommendation that the SEC eliminate the requirement that only accredited investors can invest in registered closed-end funds that invest more than 50 percent of their assets in private funds, and therefore allowing nonaccredited investors to invest in those funds. Would you guys like to take a vote on that at this time?

Okay, a motion.

PARTICIPANT: Motion.

PARTICIPANT: Second.

MS. GARRETT: Okay, all in favor.

(A chorus of ayes.)

MS. GARRETT: Opposed?

(No response.)

MS. GARRETT: Okay, thank you. So that motion passed, thank you very much.

And I think now we can also get to you talking about pooled investment vehicles. But I think it's also important to talk about ways to get money into smaller companies, smaller markets and different means to do that.

MS. HANKS: On that topic, I mean, I think what we just voted on is great for the investors. But that's not going to take the money down. As we've seen, when they're talking about small companies, they are not talking about the Blue Fish Thing Company. Sorry, I'm vegetarian; I don't eat them anyway. So but that company. That company could really do with investments from pooled vehicles.

And if we could use Reg CF, as Youngro says, there's a statutory prohibition. But Reg CF and Reg A, if there was a way to use them for micro, nano, whatever we want to call them, investment vehicles, I think that's a way of getting money to those companies.

MS. GARRETT: Can you explain that just a little more fully, what you would propose?

MS. HANKS: Yeah, so there is a prohibition. And of course, we'd have to address the fact that there is a statutory prohibition on using the regulations for investment companies. So maybe we can, I don't know, define around investment companies some way so that Regulation CF could be used for an issuer that, under other circumstances, would be deemed to be an investment company because it invests in investment securities of companies who are raising funds under Reg CF or Reg A. Does that make sense?

You like that one, or --

MR. LEE: No, no, absolutely. This is a broader point. And I really wanted to, if possible, because we have limited time, kind of what the somebody talked about. We really try to focus on solutions. Because we all know what the problems are.

And when we think about solutions, it really is the fact there is defined bodies of work, including the SEC Staff has worked so hard to come up with different examples, that if we just tweak a little bit here and there, it can -- it's not going to, obviously, solve all the problems but it does a big chunk of it.

Like, for example, I would love to hear like Jason kind of talk about his perspective. Because like -- or Jason -- for example, like there are reputable managers that we all know. Like, clearly, Jason is investing in different things, as Blackstone. Right? So that's a good thing. We kind of make the assumption.

But in other words, how do we create incentives for Jason to invest into these smaller businesses, because he has a reputation and so on and so forth. So, yeah, the issue, of course, can be tax benefits and things like that.

But I think, for example, if we change the rules of Regulation Crowdfunding slightly. So, number

one, what Sara said, making -- allowing Jason to potentially utilize Regulation Crowdfunding to bring capital from nonaccredited investors to his funds, right? Eliminating the investor restrictions -- sorry, investment restrictions, so he's not tapped out by somebody saying, hey, I got $2,000 and I'm done, even though I have $20 million in the bank, because that's what the rules are saying. Or even things like I can get compensated on different ways than what the investment is supposed to be generating.

So again -- I don't want to get too technical in this session. But, for example, Regulation Crowdfunding prohibits compensation to the actual registered intermediaries unless you're getting paid in the exact same securities that's being sold. Right? And there's no performance fees, either. So there's no incentive created to the individual or the firm that's willing to make the capital and time and investment to go downmarket and invest in these small markets which selfishly I'm saying that's what NextSeed does because the team believes in that as a philosophy, for no other word.

But there's no structural incentive to encourage that, other than saying, hey, like, do it if you want to. There's no economic incentive. That's one

of the biggest reasons why the Regulation Crowdfunding industry hasn't increased, in my opinion. Because there is no incentive for anybody with the talent or the capital or wherewithal to be able to do it, to actually make money off it. And that's a very existential question for the entire investment crowdfunding industry. Because the system and the laws literally prohibit that kind of economic incentives.

So, Jason, I just use you as an example just because of your company. But I'd love to get your perspective on these issues.

MR. SEATS: That's fine. I mean, I definitely could expand on that. But I -- I mean, the risk is to me that still feels like it's on the investor side of the marketplace. Right? I mean, where my head goes, I mean, you heard from our guests pointing out that there is the 35 nonaccredited investor limit. You can take that. But we all know why that doesn't happen. And I think one of the ideas of thinking about using pooled vehicles to help address that would be to figure out how to pool those investors in a way so that they can plug in with a different sort of disclosure requirement.

So there's some pooling that could happen below. They're talking about pooling fund of funds. You could also pool all the nonaccredited investors into

one vehicle. You treat that vehicle as a qualified purchaser or whatever else, create the right disclosure adjustments there and now all of a sudden -- those are small tweaks. And we already have vehicles we can pool them into.

We could go deep on that. I just want to make sure that we're not just having a different -- like a smaller dollar conversation, it feels like, when -- that conversation. Because is that still addressing the use of that aggregation of capital, right?

MR. FOX: To just make sure I'm understanding what you two guys are saying, I think I'm hearing you say, hey, I got the brewery in Houston that's looking to raise money. And I'm probably getting this wrong. But I'm posting them on my website with their details and they're raising money.

You're actually saying, instead of actually advertising the brewery itself, I'm actually going out and saying, you know, I'm Jason, here's my background, I want to raise some money to go invest in local businesses in the Houston and greater Texas marketplace. Here's our background. I want to raise some money and I'm going to invest it. Here's the type of investments we're going to get into. Here's my background, right? And we're going to go invest it. And you don't have to necessarily be an accredited investor because of my background, right, and I'm going to have my own money in this thing and everything else, right? And therefore, you don't necessarily have to be an accredited investor; you just invest directly into my investment vehicle, right? We go make these investments. And so we don't have to necessarily separately fund raise for the brewery. If that's a good investment, you'll just make that investment, right, through your fund.

I think that's what I'm hearing you say, right? I just want to make sure that I'm, in my own words, that I'm articulating the two different --

MR. SEATS: You got it. And I would think about the gap between where these guys are playing. And the need we see is how do we think about new fund formation in local markets.

And Youngro has got a different approach, which is the virtual local market of the digital market. You know, same difference, though. Like how do you create new fund managers --

MR. LEE: Robert, just to clarify, what I'm saying is -- you have it exactly right. And what I'm saying is, if you believe if, let's just say the direct investment is too risky. Let's just assume that's true, even though, you know, not everybody agrees with that.

But if we assume that pooled vehicle, we can live with that.

What I'm saying is that Regulation Crowdfunding provides an existing mechanism to allow that overnight, literally. If you change literally "and" to "or" and then allow pooled vehicles.

MR. SOLOMON: Yeah, that is true. And so one of the things that I thought, you know, we'll try a distinction here between what we're talking about and what Blackrock does. You know, the Blackrock presentation is a very big -- they are so big and they think about things in such a brute force way, they're not exactly connected to the day-to-day what's happening in individual communities, as much as they say they speak for the retail investor.

But the point that they made, both of them made, which was you can use existing regulations with small tweaks in order to target and focus on small funds. So if we can figure out ways to use the BDC mechanism to raise small commingled vehicles for investors that aren't necessarily accredited, that's a mechanism that we can use to essentially raise money on your platform, Youngro, or any other crowdfunding platform that effectively allows there to be a fiduciary responsibility that fits in there.

I will tell you, I hadn't frankly focused on this idea of using BDCs, because I never thought about the idea of just tweaking the BDC, the '40 Act definition. That's actually a relatively easy thing to do also.

Now, what Blackrock will be doing with it is probably nothing like what we would want to have happen in terms of capital formation and local to local or in the middle of the country. Maybe it will, maybe it won't. But it doesn't mean that the idea is a bad idea; the idea is actually a pretty good idea that others can take and figure out ways to raise money from individual investors for local investment using that format. That's actually a pretty easy change, in my opinion.

MR. SEATS: Yep, totally agree. And it doesn't have to be a BDC. If you could pool nonaccredited into an entity that can be defined as an accredited investor or qualified purchaser, then you can use the venture exemption for the pool, and you don't have to go register the firm.

MR. SOLOMON: That is also true.

I mean, I just had the situation where my son -- my son, who is not accredited, is trying to figure out how to pool most of his friends together to make investments in shows they think will ultimately make it

to Broadway. That's a different thing. But I will just say what I learned through his eyes of what he needed to do in order to raise $5 million from a group of friends to invest in shows not in New York with this idea of bringing them -- like, he can't do it. And he needs me to essentially sponsor that as an accredited individual so that the pooled vehicle becomes accredited.

It doesn't make any sense to me that that's what the rules are intended to do.

MS. MEHTA: I think you still have the problems of investor protections, though. Because it's just like investing in a fund. And then it's like, you know, it's hard to get liquidity out of a fund if there's a long investment cycle. You tend to have recyclable capital. It's -- I just think you might have the same -- you might confront the same issues.

MR. SEATS: Yes, but -- and through the lens of minor tweaks, there is a structure called a qualified venture capital fund which already exists, already can accept --

MS. MEHTA: You mean the venture capital operating exemption?

MR. SEATS: No, no, the qualified venture capital fund. The limitation is 10 million in total raise.

MS. MEHTA: Okay. Yeah, yeah, yeah. Okay.

MR. SEATS: But you can take nonaccredited investors and invest in exactly the same venture opportunities. And so within that vehicle, you already are exposing the retail nonaccredited market. And so in terms of minor tweaks, you can take that vehicle. You say that vehicle is a qualified purchaser, if it's over 5 million. Now, that can be pooled into a venture-exempt fund, it's a larger fund, and you can carve off a slice of -- right? And if you limit it -- if you increase either the number cap from 250 or the dollar cap, you could pool more people into that, right?

So I -- look, it's just an idea. But I'm just -- it's an alternative to the BDC structure which is potentially much heavier from a regulatory standpoint.

MS. MOTT: So the question around that is, that was created through legislation. Whether or not we can address it here, I don't know. Because I think the 10 million cap and the 250 investors was legislated recently.

MS. MILLER: It feels like you're looking at me again. This seems to be the theme of this afternoon.

No, you're not -- I mean, I would say to the committee, as you're thinking about these issues, I think one, there's a natural, I think, inclination to

try to find the one solution to the really big problem. With the diversity of companies and ways they're raising capital and types of investors, I think, one, there's a lot of different issues along the capital trajectory and pipeline. And one issue, whether it is closed-end funds or whether it is talking about crowdfunding, that doesn't fix the entirety of it.

So I don't think the committee should set as its objective to find the one solution this afternoon, but to rather pinpoint the various different solutions and then, you know, some of those solutions could be implemented by the SEC. Some of those may require congressional action. And I think that you each have a microphone here as a part of this committee to make recommendations and to think strategically about what the marketplace needs and to not worry about the mechanical minutiae of how you actually accomplish that.

There's a lot of technical, brilliant minds, many of whom are in this room and listening that can figure out those pieces. But to think more strategically about where the rules and the playbook needs to go as opposed to how the players are going to ultimately play the game once the rulebook is written. Does that make sense?

MR. SOLOMON: Can I just add one other thing?

And I apologize for jumping in so much remotely, but I'm going to have to jump in a minute.

The amount of money that has been raised, I'm not sure the committee knows this, but the amount of money that has been raised in BDC format over the last 10 years for direct lending is a crazy amount of money. It's dwarfed every other asset gathering mechanism because of the search for yield. And when you think about the utilization of BDCs primarily lending, so direct lending BDCs, as opposed to private equity style BDCs, it has been one of the great distribution, I think, gold rushes of all time. Whole firms were created off the back of this.

And the reason why -- you know, I hadn't really focused on why people weren't really using BDCs for private equity. What I'm saying is, there's a -- that mechanism is a relatively straightforward mechanism -- make sure we're doing everything we can for investor protection. But the reality is, I guess, for me this is an ah-hah moment.

Like, I hadn't really focused on this idea that using BDCs for some of the things that we think are really critical might be a relatively straightforward mechanism for unlocking the flow of capital. I'm going to have to explore them a little bit more. But it seems

to me that's a pretty -- that is an instrument that retail investors actually understand incredibly well because they've been investing hand over fist in debt instruments for the last decade.

MR. YADLEY: Sounds great. So here's another -- another general idea in response to Martha's challenge there.

So this morning we talked about different ways to add to the accredited investor definition by looking at knowledge. And that's one of the things in the earlier recommendations that Carl is putting together. And we talked about, although I'm not sure we reached a consensus on investment levels, except there were a couple of things. They should be harmonized and maybe it should be investment by investment as opposed to you get your one shot to put your $2,000 out there.

And beyond that, creating pooled opportunities with some proxy for vetting or analysis. As I said this morning, you can't really expect a normal person who works to be able to evaluate companies the way paid managers do. So a fund that's created by a registered investment adviser or other professional with responsibilities that -- who's regulated and has fiduciary obligations to the investors would be one path. Another path might be a lead investor or

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investors. Not sure that they should have liability for that, that they're doing it in some sort of independent way. Maybe there has to be some relationship between that lead investor and the other investors. And then a third path would be a certain amount of accredited investors, a majority of accredited investors, and then that now allows tagalong not accredited investors. That's a concept.

MR. FOX: I guess I'll pile onto that if that was a potential proposal. I like the first part of it, especially the idea of the proposal of having as a proposal for the committee to consider, you know, for the SEC and others to look into for, you know, this idea that, you know, one way to get nonaccredited investors into the marketplace is that basically, you know, some sort of professional can -- you know, some sort of regulation can be put in place, you know, for a fund, some sort of pooled investment vehicle that can be managed, whether it's BDC, qualified venture. I don't think we have to get into the sausage making, right, in terms of what it is.

MS. MILLER: No offense to our vegetarian.

MR. FOX: Yeah, sorry. Yeah, soy sausage, right. Beyond meat, here.

You know, but -- anyway, I like that idea, in

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terms of, you know, one way to get nonaccredited investors into the marketplace if they're interested, if they're out there, however it is, or even if they're accredited investors and they want to get into a diversified pool, right, because I think there's also this issue of accredited investors that really aren't investing, right? And they may also want to get into this as well. You know, I like that idea.

I'm not sure about this thing about, well, gee, if it's a majority of accredited investors, have tagalong and stuff. Because it just seems like, just because you've got a bunch of them, I'm not sure exactly what that does for you and, you know, I'm not quite sure what, you know, just because there's a bunch of them whether that's good for the rest of them. Maybe somebody could, you know, talk to me more about why that's a good thing or not. I'm just not sure exactly why that's good or bad. But I just didn't follow that one, but I like the first part of it.

MR. LEE: Hank, could I volunteer you to kind of share what you shared during lunch? Because I think this is all great from the investor perspective. But I really want to keep focusing also on really the business perspective because, right, the purpose of this committee wasn't just, oh, let's get yield to

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nonaccredited investors. It really was as much as anything else, bring capital to small businesses. And I think that's the one thing that -- I mean, that's my one -- I hundred percent support any changes to pooled investment vehicle to make it flexible.

But I think Jason raised that same point or question or Hank raised that to the speakers. Just that probably isn't going to get to the issue of actually pushing the capital down to the local businesses and small communities. So I just wanted to kind of get your perspective on that.

MR. TORBERT: You mean in particular the story I told earlier?

MR. LEE: Just, I mean, your own company and - -

MR. TORBERT: Yeah, I mean, one, I'll give you an example of a company called Dixie Beer in New Orleans, which is pretty well known. It closed some time ago. And over the last, say, 10 years, they tried to restart consistently. This is a brand that's pretty well known throughout the South, notably the New Orleans region, and could have easily restarted earlier if they had access to smaller investors. I mean, this is -- you know, it's one of the best-known brands.

Finally, in the last year, it's restarted

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because of the investment of a billionaire family. That is it. But if there was a way or a vehicle of some type that could have easily taken investors from the area, from the region, whichever, potentially it could have restarted overnight. If we can create vehicles that allow us to do that, I think you'll find a whole new creation of business and economic development throughout the region. That's the problem that I see.

And also, as someone who operates a business, same thing. We're pretty well known. But I will tell you, when talking to some private equity firms, we're too small and not worth the time or effort. Even if they do have access to capital, it's just not worth their time. But if we pooled local investors who know us and not only the people who know us in the sectors in which we operate, it would not be hard for us to pull in probably a substantial number of investors.

MR. SEATS: Yeah, to my ears, I feel like -- like I'm trying to sort and categorize this. I think there's three different dynamics that we're speaking to. One is this idea of local investor feedback loops. What are the right structures that will facilitate that? Could be digital, could be intrastate. There's lots of ways. Right? That's one.

Second is one idea that Ross brought up, is there something in between debt and equity? Is there some other type of investment structure that hits a better sweet spot of small business that currently isn't able to find capital through traditional sources? That's the second bucket.

And then I think there's a third bucket, which is the macro movement of largescale asset managers, which these guys spoke to. Right? And the dynamic there, I feel like the hundred-pound elephant in the room is the dynamic there is JOBS Act and companies staying private longer and the flow of capital towards larger pooled vehicles which then flows to larger investments. And then just the side effect of that is away from smaller pooled vehicles and smaller investments. You roll that dynamic forward for whatever, nine years or, whatever, eight years and we get to where we are.

I think those are three different lanes. Like they feel like three different things. But we sort of talk over on all of them, you know. And I guess maybe just to sort of posit for the room, I don't know which of those three is the ripest for us to try and think about what are suggestions we can make or something, you know -- I don't know. I have no proposal. This was -- I am just categorizing there's three buckets there in my

mind. On the locality, is there a different way to invest that we're missing, and then go back in time, if we didn't have JOBS Act, what would the world look like right now.

MR. FOX: But I think, Jason, there's a -- to Martha's beautiful analogy this morning, there's a whole garage of tools of, you know, bikes and everything. And, I mean, if I could go back to this, you know, professional pooled vehicle, right? I mean, you know, whether it's a better crowdfunding site, right, or whether it's just a thing where we could have kind of a broker or an attorney network or something, right? You could have a registered investment adviser in New Orleans that could say, hey, you know, I'm -- I've met the credentialing and I can go out and raise capital, right, to go set up to raise the 5 million bucks I need to -- that we need to get Dixie Beer off the ground, or whatever it is. Then I think we can solve -- I mean, and if it's more money, there's a lot of different ways.

I just feel like, you know, to me, I think what we need -- there are some gaps. Right? But I think that there are, you know -- we can't lose sight of the fact that capital is being raised every day, too.

MS. MILLER: Can I just jump in? Because I'm going to take that analogy and I'm going to reuse it and

I'm going to reuse it terribly. But here we go.

So as you think about kind of, we have all of these different vehicles that you can take. And as we were talking about, I think, Youngro, to your question of, Hank, how do we think about this from the perspective of companies that are raising capital? If you use my terrible garage analogy, most people don't start out in the morning and think, I'm going to take a bike ride today. They think, I'm either going to take a bike ride for exercise, or it's a clear day and I can bike to work, or I'm going to get in the car because I have a trip that's further out of town.

The destination, how far you need to go and your capabilities for it are what drive it, as opposed to you randomly selecting the vehicle that sounds nice that day. And I think that a lot of what is easy to do in the securities world is to get hyper focused on designing great vehicles and to not think about where the passenger is ultimately going and choosing to drive and where do they need to be.

So as we think about this, I would encourage people to step even further back from some of the different nuance of how do we tweak different -- you know, should we be tweaking this fund or that fund structure and instead think about, kind of, if you're a

company, the first thing you're thinking about is how much money do I need? That's the first thing you usually think about. You have a dollar amount that you know you need. The next thing is, who can I raise it from, figuring that out. And then how do I reach them, what are the tools to reach them?

And generally, only after you've figured those elements out do you actually start thinking about regulatory exemptions and what are the obligations within each. And so I think if we can kind of reverse engineer the way that we're thinking about it and thinking about how much money do you need goes into do we have the ability to raise the right amounts across the different exemptions we have? This really goes to the broader picture of harmonization.

Can you raise what you need using the tools? Can you go the distance on that vehicle as it's designed? Does it have a limitation on it that doesn't make sense for how far you need to take it?

And the next one is looking at the investors, can the right people that you have access to actually support you on that path? And then what tweaks do we need to make sure that that is a more efficient journey?

That's how I think about it. I don't know the extent to which that's helpful. But I think that draws it back to why we are actually talking about accredited investor. It goes directly to who do you have access to as often your kind of first line investors? The pooled vehicles that we're talking about are often -- they're not the first dollars into a company. They're very valuable at a different point in the journey. It's not that they're not important. I think that we just have to be thinking about the holistic picture of how companies are raising capital. That is what harmonization goes to, is looking at from first dollars to IPO, what does that path look like across the exempt framework to allow you to raise what you need?

MS. MOTT: A lot of companies never go to IPO. And so I'm glad you brought that up.

Where I see the biggest gap in the market is in that point where you're trying to scale beyond the region, you're trying to get into the next, you know, the next region. Or you're trying to export your products and services. And the classic example of success in venture capital most of the time really is merger and acquisition, not IPO.

And so the other thing I want to bring up is, as we think about this, I just -- I'm really sensing I need a lot more time. But is that a lot of people who

are managing venture funds are operators, they're not RIAs. These are people who -- in the funds that I look at and I see that I aspire to are the ones where they have a group of people who act as entrepreneurs in residence or mentors or whatever to help that company navigate the growth issues that they're going to have, deal with their strategy, you know, manage the obstacles and try to conserve cash while you're -- while you're doing this because you're going to make mistakes. That's the point where I see we need the most amount of money.

I mean, it's like we're great, we get started with crowdfunding, we get started with angels, that kind of thing. But where we really need to take this company is the next level. And you -- what they're trying to do is get -- you know, compete with Silicon Valley and Boston and New York City. And too much money is chasing -- I mean, they're all chasing the same deals, which is why they're in the situation they're in right now with unicorns and things like that.

So I guess when we say this, when we look at the different tools that we might have in our toolbox, what could really address that major gap is what I'm thinking about.

MR. YADLEY: So one of the responses, Martha,

is general solicitation and offers and the focus away from that and to purchasers and -- because that's matching and accessibility and 506(c) has not been used as much as people thought, presumably because of the verification. But maybe that's not it.

I've had -- sort of before we even got to the verification, a client that tried to find investors for a pretty appealing, romantic kind of investment. Not that kind of romantic. But, I mean, like -- and couldn't find the interest from people that he didn't know.

So I don't know if that's it or not. But certainly we could debug a bugaboo, or we might find that that's a way, especially on local deals, for people to be able to communicate. And that would help under 506(b) and 4(a)(2).

MS. GARRETT: Sara, did you want to talk a little bit about that?

MS. HANKS: Yeah, well, on the subject of offers, since we've only got a short amount of time, I'll be brief. But just to sort of go back to the beginning of the regulation of offers, since 1933, Section 5 of the Securities Act has said, if you make an offer or sale of securities, that offer or sale has to be registered or exempt.

That means that the U.S. is kind of an outlier compared to pretty much everybody else in the universe in regulating just making an offer by everybody. That offer has to have an exemption applicable to it at the time that it's made. And that has the result of regulating what you can say and who you can say it to and what else you have to deliver in terms of information at the time of the offer. And as all of these offers have moved onto the internet, that's got -- that's had an impact on the delivery of information and how do you get information into the hands of investors at the time that you're supposed to?

One of the problems that we're seeing is, when you put together the fact that everything is an offer, still -- and I love quoting this Securities Act release because it's one of the few things around here that's older than I am. October 1957, there is a statement that says, what is an offer of securities? It is anything that conditions the market. Anything that makes people kind of interested in the offering that's going on.

So starting with the point that everything is an offer and then going on to the point that every offer has to be registered or exempt at the time it is made. Bringing this forward 62 years, we're now in the situation where I've got clients who are saying, okay, we want to publicize the offering on TikTok, real case. Or we want to publicize the offering within the videogame. We're a videogame company and we want to be able to, in the videogame, say do you like playing this videogame? If you like playing this videogame, you should buy the shares, which are available on Regulation CF.

Because at that time you have information delivery requirements, it means it's incredibly difficult to comply with the regulations. And so one of the proposals that at least that I would urge is maybe we don't focus on regulating the offer. It would be possible to say that if you -- if the sale is compliant at the time of sale, then the offer gets to be exempt at the same time.

Another thing, I just want to throw in here --

MS. GARRETT: Sara, real quick, because I think we have two people that need to leave. And if the committee wanted to, we could do a quick recommendation in terms of the accredited investor definition before people leave?

PARTICIPANT: Yeah, let's do it.

MS. GARRETT: So what I've written down from earlier today is that the committee makes the following

recommendation with respect to the accredited investor definition: To leave the current accredited investor financial thresholds requirements in place subject to the SEC adjusting such thresholds possibly downwards for certain regions of the country, and to index the financial thresholds for inflation on a periodic basis, and to look into revising the accredited investor definition to allow individuals to qualify as accredited investors based on measures of personal sophistication, which could be bright-line rules for being an accredited investor by sophistication, which could include -- sorry -- professional credentials, work experience, education and/or sophistication test.

Can I have a motion or would you like a discussion on that. Or a motion?

MS. MOTT: So moved.

MS. GARRETT: Okay. And all in favor?

(A chorus of ayes.)

MS. GARRETT: And all opposed?

(No response.)

MS. GARRETT: Thank you.

Sara.

MS. HANKS: That was pretty much it for the offer regulation. Although the one thing that we should consider is if you are going to deregulate offers, does

that automatically mean that you are now throwing out all prohibitions on general solicitation? Not everybody sees it the same way.

I think that if you're deregulating offers, you are inherently deregulating manner of offering limitations. But not everybody sees it that way. So we should be specific when we address it.

MS. GARRETT: Thank you.

So we have a handful of other, I mean, points that we've talked about. We've talked about the pooled investments. We haven't come to the recommendation on that yet. We've talked about the crowdfunding; we've talked about regulation of offers. Is there anything specific that anybody would like for me to propose as a recommendation?

MR. SEATS: I mean, the regulation of offers feels like a general consensus item to me. I don't know, maybe it's not. Are there -- every time it's come up, I feel like we all sort of have the same orientation on that one. I don't know. No?

MS. HANKS: Certainly on this committee. The other committee --

MR. LEE: Just to be clear, when we say no regulation, there's still, no matter what, there's antifraud laws, there's inherent rules that govern --

like, you can't lie, no matter what, right?

So I think it's really, what Sara was explaining as an example, for example, Regulation Crowdfunding, I think you an only say -- it's called a tombstone rule. You can say certain things and you can't explain anything. So every other month, we get a call from FINRA and it's like this offer had this other word about, you know, the terms or whatever. You're not allowed to say that. So I'm sure they don't want to spend the time reviewing that. I'm sure a lot of platforms, they sure don't want to go through that.

But that's an example of, right, like what's the point? When the ultimate thing is, if you buy, then you better have complied. And if you didn't buy, then who cares?

MS. HANKS: And all of that compliance can take place at the time of sale. You can dictate that prior to sale, there must have been delivered all of the things that need to be delivered. You can also dictate, as you say, antifraud doesn't change at all. If you lie, you're liable for it, exempt or not. And you just make sure that the delivery of information happens at the time -- prior to the time of sale.

MS. GARRETT: It sounds like what we're saying that we would recommend that the SEC look at revising the exemptions across the board to focus consistently on investor protections at the time of sale, rather than at the time of the offer, so that the offer would be exempted. Okay.

So we don't have a quorum, but we did propose --

MS. DAVIS: Is anyone still on the phone?

(No response.)

MS. DAVIS: Okay, we don't have a quorum anymore.

MS. GARRETT: What were you -- is there a way to

MS. MILLER: So one of the things that I was briefly whispering to Carla is this is a big issue. There's a lot of -- I think we've talked about a lot of weighty topics and I think most people think like they are still processing a lot of it. And we do have the option to reconvene between now and our next meeting, telephonically. That is very much so an option if we would like to do so. So I just -- I offer that up as something that is available. It would be something that would be accessible. Members of the public would be able to listen into the call. It would comply with the same sunshine and other requirements for it. So I just share that as an option, so that people don't feel the

pressure to come to consensus on longstanding topics.

Yes, Mark.

MR. SHARMA: Thanks, Martha. I would like to add to that. And based on my experience with the Investor Advisory Committee, I would like to remind this committee that you do have access to the Staff of the SEC and all the experts in the building. So to the extent that there are unanswered questions you think it would be helpful to have a briefing or a phone call with certain Staff, that is something we can arrange for you.

COMMISSIONER PEIRCE: And I would just add to that that, again, what's most valuable to me as a commissioner is to get your views on what it's like in the real world. So sometimes when you do talk to the Staff, you might get drawn into the legal nuances. But what we really need to know is what are the practical obstacles you're facing in the real world? And Martha, I think, laid this out really well.

We can worry about then trying to deal with how does that fit into our regulatory and statutory framework. But knowing what you're running into and what doesn't make sense to you is really valuable to us.

MR. LEVEY: I think --

MS. MEHTA: I think -- sorry. No, I mean, I would love to table the decision on whether to separate

offers and sales. Because I do think general solicitation is too broad as it is. I know we've discussed it before. But things like, you know, pitch competitions and conditioning the market is very broad. And so I do think that needs to be addressed. But whether to get rid of it altogether, I don't know that -- I'm certainly not ready to make that decision without digesting more information. So I would just vote to table that for now.

MR. LEVEY: And from my perspective, having just taken a company public, you know, just how that could affect some gun jumping and conditioning the market in the context of an IPO and all of the precedent that's there on that topic. I just -- not being an expert in this area, necessarily, how would any changes there affect, you know, or have any unintended consequences on sort of gun jumping rules in general? Or would it, you know, eliminate them in total? Possibly.

MS. GARRETT: Okay, thank you.

And since we don't have a quorum, we can't vote on these items. So I think it would be a good idea to continue the meeting and have an interim meeting, if people are interested in that, where we could discuss some of these ideas a little bit more fully. And Martha

can advise us how to do that.

MS. MILLER: We will be in touch.

WRAP UP AND ADJOURNMENT

MS. GARRETT: With that, we can either continue talking about some of the items, or we could, you know, decide to adjourn for the day because we have lost some members of the committee.

MS. MILLER: I did want to make sure we did one bit of news about one committee member. Did you want to share that?

We have one committee member who has changed employers and the 8-K is out. Terry McNew has been lured to a new wonderful position. And so with that new position, he has resigned from MasterCraft Holdings as well as from this committee.

I just wanted to make sure we thank him for his service on the committee. He certainly brought a colorful and spirited perspective from the perspective of a small manufacturer in Tennessee, which we have appreciated. We wish him well in his next venture.

MS. GARRETT: Thank you very much.

MS. DAVIS: And I have one piece of admin. Everyone probably noticed, and we put this on the web, too, that we had a PowerPoint from the Federal Reserve Bank of New York that has a lot of stats from their small business credit survey in 2018. A lot of the stats are somewhat similar to what Kauffman presented but there is even more in here. And we invited them to come participate today and present, but they were not -- they had a scheduling conflict.

So we thought the stats were worthy of people's eyes and so we wanted to pass it out and put it up as part of the record.

MS. GARRETT: Okay. Well, thank you very much. Our next meeting will be a telephonic meeting, which we will schedule. And then our next in-person meeting will be February 4 here in Washington, D.C. Thank you, everybody, for your participation and, with that, I move to adjourn the meeting.

(Whereupon, at 3:24 p.m., the meeting was adjourned.)

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PROOFREADER'S CERTIFICATE

In the Matter of: SEC'S SMALL BUSINESS CAPITAL FORMATION MEETING

File Number: OS-1112

Date: Tuesday, November 12, 2019

Location: Washington, D.C.

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

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I, Beth Roots, reporter, hereby certify that the foregoing transcript is a complete, true and accurate transcript of the matter indicated, held on __11/12/2019___________, at Washington, D.C. in the matter of:

SMALL BUSINESS CAPITAL FORMATION.

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

Date: 11/12/2019

Official Reporter: Beth Roots

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