Should the Commission Revise the Accredited Investor Definition?

SEC Government-Business Forum on Small Business Capital Formation

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http://www.gew.co/gbad
Angel Capital Association

World’s Largest Association of Accredited Angel Investors

www.angelcapitalassociation.org

- 12,000+ individual accredited investors
- 220+ angel groups and accredited platforms
- Voice of accredited angels
  - Best practices
  - Public policy

Mission: to fuel success of angel groups and accredited investors and the early-stage companies they support
Accredited Investor Definition

- Regulatory objectives
  - Investor protection
  - Streamline capital formation for small business
  - Maintain market integrity
- ACA goals
  - Preserve ability of knowledgeable investors to fund startups essential to job creation
  - Prevent undue obstacles to investor/entrepreneur relationship
  - Provide accredited investors education and best practices to enhance sophistication
Angels Drive Most Startup Funding

• In 2013, angels invested $25 billion in 71,000 companies
• Majority of net new jobs in US are from companies < 5 years old
  • High-growth startups create most of these jobs
  • Many receive angel funding prior to any VC investment
• Angels provide 90% of outside equity raised by startups
  • Virtually the only source of seed funding
  • 90%+ of VC goes for company expansion
• Angels deploy own funds and make own investment choices
• Approximately 200K-300K active angel investors
Where Angels Invest

Q2 2014 Share of Angel Group Deals by Region

- Northwest: 5.9%
- Great Plains: 3.9%
- Great Lakes: 9.3%
- New York: 8.8%
- New England: 15.6%
- California: 19.0%
- Southwest: 6.8%
- Mid-Atlantic: 11.2%
- Southeast: 7.8%
- Texas: 11.7%

Angel Capital Association

Silicon Valley Bank
Angel Resource Institute
CB Insights
HALO Report
Angel Investing = Hands-On Work

• Not just a check – ongoing support of entrepreneur
  o Customer acquisition
  o Personnel
  o Develop strategy
  o Resources: office space, accounting, etc.

• Work hand-in-hand
  o Economic development
  o University tech transfer
  o Startup accelerators/incubators

• Active deal/risk assessment
  o Deal screening
    ▶ Typically reject 90% that apply
    ▶ Potential for growth/value creation
    ▶ Fraud almost never an issue
  o Extensive due diligence
  o Negotiated terms – issuer does not set
    ▶ Information rights
    ▶ Board or observer seat
  o Intermediaries not involved

• Accredited platforms
  o Investors may follow a successful lead investor
Impact of Raising Thresholds - $2.5M / $400K

% of ACA members who would not qualify

Nationwide, nearly 60% of accredited investors would cease to qualify
(Source: GAO)

Map Data Source: ACA Member Survey, December 2013-January 2014
506(c) Issuer Verification Complicates Process

- Did issuer “solicit”?  
  - University tech fair  
  - Economic development event  
  - Accelerator pitch day

- Is investor accredited?  
  - Financial thresholds – who will verify?  
    - Reluctant 3rd parties  
    - Investor privacy; data security; expense  
  - Sophistication  
    - Degree?  
    - Work experience?  
    - Established angel group member?

Many groups will ONLY consider 506(b) – negating JOBS Act intent
ACA Recommendations

• Leave financial thresholds alone
  – Clearly understood and worked well for decades
  – Removal of primary residence (2010) was significant shift
  – Private market too large and vital to further restrict investor access

• Add sophistication criteria to expand class
  – Membership in an Established Angel Group™
  – Previous experience with Reg D offerings
  – Prior board, executive, or financial responsibility
  – Relevant degree or training: ACA certificate, MBA, JD, CPA, CFA, etc.

• Enable investors to certify via detailed questionnaire
  – Validates sophistication
  – Satisfy “issuer verification” for 506(c) deals