U.S. Securities & Exchange Commission’s
Office of the Advocate for Small Business Capital Formation

Overview of FY2020 Annual Report
January 29, 2021

Disclaimer: The views expressed in this presentation are the speakers’ own and do not necessarily reflect those of the Commission, Commissioners, or Commission Staff.

Direct report download [here](http://www.sec.gov/oasb).
Presentation Preview

- Highlights from FY2020
- Capital Raising Trends
  - Demographic Trends
  - COVID-19 Impacts
- Policy Priorities
  - Challenges of Offering Complexity and Friction
  - Bridging Networks between Founders and Investors
  - Diversifying Access to Capital
  - Attractiveness of Public Markets
- Q&A
FY2020 was a busy year…

**Q1 FY2020**
- Office joins Inside the Icehouse for first podcast recording.
- National Veterans Small Business Coalition, Keynote address on trends and opportunities for Veteran entrepreneurs and solicitation of feedback.
- Keynote address at National Venture Capital Association’s Strategic Operations & Policy Summit.
- HBCU Outreach Event at Morehouse College. Panel discussion on best practices for minority businesses to attract investment capital.
- California Bay Area Listening Tour. Attended AfroTech, met with founders, investors, and other key players in early-stage and growth capital infrastructure.
- Roundtable with Miami entrepreneurs and investors on raising capital in partnership with the Miami-Dade Beacon Council.
- Joined Institute of Management Accountants Small Business Committee Meeting to discuss top accounting issues faced by advisors to small businesses.

**Q2 FY2020**
- Office hosts its first Capital Call styled after earnings release calls to explore inaugural annual report.
- Kenan Institute Frontiers of Entrepreneurship Conference. Panel discussion with academics and thought-leaders on JOBS Act and small business capital formation.
- Brooking Institution’s “The Devaluation of Businesses in Black Communities” panel discussion on challenges faced by business owners in minority communities in accessing capital.

**Q3 FY2020**
- Virtual Coffee Break: Online investment capital raising. Discussion for small businesses and investors considering new strategies to bridge their networks.
- Virtual Coffee Break with National Small Business Association. Discussion with businesses from a wide range of industries on what they are seeing in the market.
- Virtual Coffee Break with National Diversity Coalition and U.S. Small Business Administration. Discussion on how COVID-19 is impacting raising capital.
- Workshop with iFundWomen to walk through pathways available to access investment capital.
- Entire SEC Small Business Forum conducted virtually.

**Q4 FY2020**
- Virtual Policy Discussion: Policy and business with Middle Market Private Companies & Late-Stage Investors. Discussion on the experience of small, public companies traded over the counter.
- Virtual Panel Discussion on Small Businesses in the Public Markets. Discussion on the challenges of minority communities in accessing capital.
- Keynote speech at Angel Capital Association Summit. Discussion with angel investors from across the country.
- Office hosts its first podcast, Icehouse Inside the Office joins on trends and services. Some of the events in which we have engaged this year include:

**Highlights from Fiscal Year 2020**

**Q1 FY2020**
- Keynote speech at National Venture Capital Association’s Strategic Operations & Policy Summit.

**Q2 FY2020**
- Office hosts its first Capital Call styled after earnings release calls to explore inaugural annual report.

**Q3 FY2020**
- Kenan Institute Frontiers of Entrepreneurship Conference. Panel discussion with academics and thought-leaders on JOBS Act and small business capital formation.

**Q4 FY2020**
- Entire SEC Small Business Forum conducted virtually.
Small Business Capital Formation Advisory Committee FY2020 Summary

The Small Business Advocate Act established the SEC’s Small Business Capital Formation Advisory Committee. In April 2019, the Commission appointed the inaugural members of the Committee. The Committee provides a formal mechanism for the Commission to obtain the views of small businesses, from emerging, privately-held companies to publicly-traded companies, on issues affecting small businesses, and to consider actions that may affect the ability of such small businesses to raise capital in capital markets. Committee members meet at least five times per year, with additional meetings called as necessary. The Committee is comprised of 25 members, appointed by the Commission in FY2020 to fill vacancies: Kesha Cash and Sue Washer. In addition, Melanie Senter Lubin succeeded Michael Pieciak’s service as the SEC’s Advocate for Small Business Capital Formation.

Committee FY2020 Summary

The Committee met at least five times during FY2020 to receive, hear, review, and consider recommendations related to small businesses. Minutes from meetings, excluding agenda, presentations, and final actions, are available on the Committee’s webpage.

Small Business Capital Formation Advisory Committee FY2020 Meetings

- November 12, 2019: Harmonization of the Exempt Offering Framework and Proposed Investment Funds
- December 11, 2019: Harmonization of the Exempt Offering Framework (continued)
- February 4, 2020: Exploration of Small Business Capital Markets Data and Challenges Facing Small Businesses and Their Investors; and the Role of Regional Funds
- April 2, 2020: Challenges Facing Small Businesses Due to the COVID-19 Pandemic
- May 6, 2020: Underrepresented Founders and Investors
- August 4, 2020: Challenges Facing Small Businesses Due to the COVID-19 Pandemic (continued)

Committee Recommendations

During FY2020, the Committee put forward the following six recommendations to the Commission:

1. Harmonize the Exempt Offering Framework and Proposed Investment Funds
2. Establish a Small Business Capital Formation Advisory Committee
3. Revise the definition of “accredited investor” under Regulation D of the Securities Act of 1933 (Securities Act), the Commission
4. Create a comprehensive database of publicly available information
5. Clarify the role of regional investment funds
6. Establish a mechanism to address underrepresented founders and investors

The Committee’s FY2020 Summary is available for download at: [Committee FY2020 Summary](#).
Meet our team of advocates:
Data Sources

Unless otherwise indicated, data is derived from public filings with the SEC, as analyzed by the SEC’s Division of Economic and Risk Analysis.

Full citations, explanations of, and links to referenced data are provided in the annual report, available at www.sec.gov/oasb.
CAPITAL RAISING TRENDS
What regulatory pathways are companies using to raise capital?\textsuperscript{6}

- **Rule 506(c)**
  - \$69B
  - \$900,000 median

- **Initial Public Offerings**
  - \$60B
  - \$150M median

- **Rule 506(b)**
  - Private Placements
  - \$1.4T
  - \$1.8M median

- **Regulation A**
  - \$1.3B
  - \$2.1M median

- **Crowdfunding**
  - \$88M
  - \$100,000 median

- **Other Exempt Offerings**\textsuperscript{7}
  - \$1.2T

Source: See FY2020 Report p. 11.
Where is capital being raised?

The following maps illustrate the concentration of estimated total capital raised under various different offering types by issuers that report a primary location in the U.S., with the number of offerings conducted indicated on each state.

Where are companies raising capital?

The following maps illustrate the concentration of estimated total capital raised under various different offering types by issuers that report a primary location in the U.S., with the number of offerings conducted indicated on each state.

Where is capital being raised?

Regulation A

Source: See FY2020 Report p. 15.
Where is capital being raised?

Registered Offerings

$0 - $300 MILLION
$300 MILLION - $5 BILLION
$5 - $20 BILLION
$20 - $150 BILLION

Source: See FY2020 Report p. 15.
DEMOGRAPHIC TRENDS
Who are new entrepreneurs by race and ethnicity?

- **White**: 58%
- **Hispanic/Latino**: 23%
- **African American/Black**: 10%
- **Asian American Pacific Islander**: 7%

What percentage of employer firms are owned by minorities?

Minority-owned businesses face challenges accessing bank capital, leading to more financial restraints:

- More likely to use personal funds as primary funding source
- More likely to use personal funds in response to financial challenges
- Generally lower credit approval ratings
- Less frequently approved for full amount of loans

Minority founders raise less venture capital by headcount

23% of VC-backed founders are African American/Black, Hispanic/Latino, Middle Eastern, or Asian American.

However, when diverse teams do raise, they tend to raise more than all white teams:

<table>
<thead>
<tr>
<th>Series</th>
<th>Median Amount Raised (in Millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Seed</td>
<td>$1</td>
</tr>
<tr>
<td>Series A</td>
<td>$6</td>
</tr>
<tr>
<td>Series B</td>
<td>$13</td>
</tr>
<tr>
<td>Series C</td>
<td>$19</td>
</tr>
<tr>
<td>Series D</td>
<td>$29</td>
</tr>
<tr>
<td>Series E</td>
<td>$40</td>
</tr>
</tbody>
</table>

The 13 million women-owned businesses include:

- **White**: 6,525,946 (51%)
- **African American/Black**: 2,681,179 (21%)
- **Latina/Hispanic**: 2,346,190 (18%)
- **Asian American**: 1,169,348 (9%)
- **Native American/Alaska Native**: 180,316 (1%)
- **Native Hawaiian/Pacific Islander**: 40,375 (0.3%)

Women founders raise less venture capital by headcount

3% of dollars went to women-only founding teams, and 9% went to women/men co-founding teams.

Women-led founding teams raise less than their male peers

Lower median VC pre-money valuations in 2019


Lower median funding rounds in 2019
IMPACTS OF COVID-19 ON CAPITAL RAISING
Small businesses declined by 27% from January to September 2020.

From January 2020 through September 2020, the number of small businesses decreased by 27%.

The below map illustrates the percentage change across the country.

Between -30% and -43%
Between -25% and -30%
Between -20% and -25%
Between -13% and -20%
No data

During the same time period, how did the percentages of open small businesses change across different industries?

Leisure and Hospitality
Retail and Transportation
Education and Health Service

Revenues declined dramatically after March 2020

Of the businesses still open, how have their revenues changed during COVID-19 when compared to January 2020?

Access to capital remains a major concern for small businesses.

Many small businesses entered the pandemic with enough cash on hand to cover two weeks or less without revenue.

45% of small businesses needed to reduce their headcount.

Of small businesses planned to use personal savings to reopen their business, and 39% did not know where they would access capital to reopen.

70% of small businesses are concerned about financial hardship due to prolonged closures and 58% worry about having to permanently close.

COVID-19 has highlighted and exacerbated preexisting inequities among historically underrepresented founders.

POLICY PRIORITIES:

Challenges of Offering Complexity and Friction
Bridging Networks between Founders and Investors
Diversifying Access to Capital
Attractiveness of Public Markets
Policy Priority 1

Challenges of Offering Complexity and Friction
Small businesses less than one year old have an outsized impact on job creation:

10% of all businesses

20% of all new jobs

What are common sources of capital for small and emerging businesses?

Retained Business Earnings 77%
Personal Funds 14%
External Financing 9%

- Loan or Line of Credit - 54%
- Credit Card - 53%
- Trade Credit - 12%
- Leasing - 11%
- Equity Investment - 6%
- Merchant Cash Advance - 5%
- Factoring - 3%
- Other - 2%

Collateral is often a pre-requisite for small businesses seeking bank financing

<table>
<thead>
<tr>
<th>Collateral Type</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Personal Guarantee</td>
<td>59%</td>
</tr>
<tr>
<td>Business Assets</td>
<td>49%</td>
</tr>
<tr>
<td>Personal Assets</td>
<td>31%</td>
</tr>
<tr>
<td>No Collateral Required</td>
<td>17%</td>
</tr>
<tr>
<td>Future Sales</td>
<td>8%</td>
</tr>
</tbody>
</table>

Our rules are complex. Period.

<table>
<thead>
<tr>
<th>Type of Offering</th>
<th>Offering Limit within 12-month Period</th>
<th>General Solicitation</th>
<th>Issuer Requirements</th>
<th>Investor Requirements</th>
<th>SEC Filing or Disclosure Requirements</th>
<th>Restrictions on Resale</th>
<th>Presumption of State Registration and Qualification</th>
</tr>
</thead>
<tbody>
<tr>
<td>Section 4(a)(2)</td>
<td>None</td>
<td>No</td>
<td>None</td>
<td>Transactions by an issuer not involving any public offering. See SEC v. Razboi &amp; Co.</td>
<td>None</td>
<td>Yes, Restricted securities</td>
<td>No</td>
</tr>
<tr>
<td>Rule 506(b) of Regulation D</td>
<td>None</td>
<td>No</td>
<td>&quot;bad actor&quot; disqualifications apply</td>
<td>Unlimited accredited investors</td>
<td>Form D</td>
<td>Yes, Restricted securities</td>
<td>Yes</td>
</tr>
<tr>
<td>Rule 506(c) of Regulation D</td>
<td>None</td>
<td>Yes</td>
<td>&quot;bad actor&quot; disqualifications apply</td>
<td>Unlimited accredited investors</td>
<td>Form D</td>
<td>Yes, Restricted securities</td>
<td>Yes</td>
</tr>
<tr>
<td>Regulation A: Tier 1</td>
<td>$5 million</td>
<td>Permitted, before qualification, testing-the-waters permitted before and after the offering statement is filed</td>
<td>U.S. or Canadian issuers Excludes blank check issuers, registered investment companies, business development companies, issuers of certain securities, certain issuers subject to a Section 12(j) order, and Regulation A and reporting issuers that have not filed certain required reports</td>
<td>&quot;Bad actor&quot; disqualifications apply; No asset-backed securities</td>
<td>None</td>
<td>Form 1A, including two years of financial statements</td>
<td>No</td>
</tr>
<tr>
<td>Regulation A: Tier 2</td>
<td>$75 million</td>
<td>Permitted in limited circumstances</td>
<td>Excludes blank check issuers, Exchange Act reporting companies, and investment companies</td>
<td>&quot;Bad actor&quot; disqualifications apply</td>
<td>No investment limits for accredited investors</td>
<td>Form 1A, including two years of audited financial statements Annual, semi-annual, current, and 10-K reports</td>
<td>No</td>
</tr>
<tr>
<td>Rule 504 of Regulation D</td>
<td>$10 million</td>
<td>Testing the waters permitted before Form C is filed</td>
<td>Excludes non-U.S. issuers, blank check companies, Exchange Act reporting companies, and investment companies</td>
<td>&quot;Bad actor&quot; disqualifications apply</td>
<td>No investment limits for accredited investors</td>
<td>Form C, including two years of financial statements that are certified, reviewed or audited, as required Progress and annual reports</td>
<td>12-month resale limitations</td>
</tr>
</tbody>
</table>

- **Regulation Crowdfunding: Section 4(a)(5)**

- **Intrastate: Section 3(a)(11)**
  - No federal limit (generally, individual state limits between $1 and $5 million)
  - Officers must be in-state residents
  - In-state residents "doing business" and incorporated in-state; excludes registered investment companies
  - Officers and purchasers must be in-state residents
  - None
  - Securities must come to rest with in-state residents

- **Intrastate: Rule 147**
  - No federal limit (generally, individual state limits between $1 and $5 million)
  - Officers must be in-state residents
  - In-state residents "doing business" and incorporated in-state; excludes registered investment companies
  - Officers and purchasers must be in-state residents
  - None
  - Yes, Resales must be within state for six months

- **Intrastate: Rule 147A**
  - No federal limit (generally, individual state limits between $1 and $5 million)
  - Yes
  - In-state residents and "doing business" in-state; excludes registered investment companies
  - Officers must be in-state residents
  - None
  - Yes, Resales must be within state for six months

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Recommended Solution 1

Targeted Educational Programs
Policy Priority 2

Bridging Networks Between Founders and Investors
Angel investors play a critical role funding early-stage small businesses

323,365
active angel investors

$23.9 billion
in total angel investments

63,730
entrepreneurial ventures received angel funding

$374,225
average angel funding round

Networks barriers are among the top 3 challenges facing aspiring entrepreneurs.
Proximity to investors matters

- 37 miles to lead angel investor
- 100 miles to seed financing
- 400 miles to later-stage VC

70% of VC funds are concentrated in 3 metro areas:

Rural businesses face particular challenges raising capital. Over the three years ending June 30, 2020, businesses in rural areas raised less capital relative to the U.S. population than the national average.

The concept of ‘locavesting’—which refers to community investing—is especially important in rural areas lacking investment capital, as such areas often have strong economic ties to their local businesses.

Where are rural businesses growing in number? In 2018, 53% of rural counties in the U.S. saw an increase in the number of businesses. Rural counties in the Western U.S. led the growth, where the number of businesses increased by 2.4%. The five states with the highest rates of rural business growth were: California, Oregon, Utah, Hawaii, and New Mexico.
Artificial boundaries between investors and businesses reinforce pattern matching

Founders are **21%** more likely to be funded by an investor of the same ethnicity than of a different ethnicity.

Recommended Solution 2

Clear Finders Framework
Policy Priority 3

Diversifying Access to Capital
Late stage venture capital activity is thriving

How are mature and later-stage companies and their investors responding to COVID-19? While some funds and portfolio companies have been significantly impacted by the pandemic, initial data suggest that the VC industry in the aggregate has been less affected than other parts of the economy. A primary impact of the pandemic has been market uncertainty that is substantially different from the type of uncertainty these founders and investors have historically evaluated. Companies have been preparing for long-term impacts by establishing cash reserves and trimming budgets.

How has the pandemic impacted VC deal activity? While early-stage VC (Series A and B) started to increase in deal value at the beginning of 2020, deal count continues to decline:

<table>
<thead>
<tr>
<th>Quarter</th>
<th>2019 Deal Value ($B)</th>
<th>2020 Deal Value ($B)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Q1</td>
<td>$20.6</td>
<td>$21.5</td>
</tr>
<tr>
<td>Q2</td>
<td>$21.5</td>
<td>$20.0</td>
</tr>
<tr>
<td>Q3</td>
<td>$20.0</td>
<td>$18.6</td>
</tr>
<tr>
<td>Q4</td>
<td>$18.6</td>
<td>$22.8</td>
</tr>
<tr>
<td>Q1</td>
<td>$22.8</td>
<td>$28.9</td>
</tr>
<tr>
<td>Q2</td>
<td>$28.9</td>
<td>$662</td>
</tr>
</tbody>
</table>

First time funds continue to decline

How has VC fundraising activity changed?
Through the third quarter of 2020, overall fundraising activity remained active. However, since the pandemic hit, there has been a significant drop in first-time funds, which raised only $1.9 billion across 30 funds through Q3 2020, compared to $5.3 billion over 81 funds in 2019:

How has exit activity changed?
Over the last three quarters, acquisition activity has dropped while IPO activity has increased by deal count:

Women and minorities are underrepresented among angel investors

29% of angel investors in 2019 were women

7% of angel investors in 2019 were minorities

Women and minorities are also underrepresented among VC investment partners

Recommended Solution 3

Support for Pooled Investment Vehicles
Policy Priority 4

Attractiveness of Public Markets
How has the prevalence of publicly traded companies changed over time?

What is the scale of public vs. private investments?

As of the end of 2019, the market cap of U.S. public equities was $37.7 trillion.

- 27x the AUM for private buyout funds
- 80x the AUM for VC funds

Exit trends have begun shifting towards IPOs

<table>
<thead>
<tr>
<th></th>
<th>Acquisition (Q1)</th>
<th>Acquisition (Q2)</th>
<th>Acquisition (Q3)</th>
<th>Acquisition (Q4)</th>
<th>IPO (Q1)</th>
<th>IPO (Q2)</th>
<th>IPO (Q3)</th>
<th>Buyout (Q1)</th>
<th>Buyout (Q2)</th>
<th>Buyout (Q3)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2019</td>
<td>205</td>
<td>213</td>
<td>200</td>
<td>191</td>
<td>188</td>
<td>128</td>
<td>110</td>
<td>15</td>
<td>56</td>
<td>47</td>
</tr>
<tr>
<td>2020</td>
<td>47</td>
<td>63</td>
<td>56</td>
<td>49</td>
<td>43</td>
<td>25</td>
<td>38</td>
<td>14</td>
<td>34</td>
<td>19</td>
</tr>
</tbody>
</table>

What is happening with IPO activity?

Source: See FY2020 Report p. 27.
Recommended Solution 4: Foster the Public Company Environment

Direct report download [here](http://www.sec.gov/oasb).
Q&A

www.sec.gov/oasb
smallbusiness@sec.gov