U.S. SECURITIES AND EXCHANGE COMMISSION

SMALL BUSINESS
CAPITAL FORMATION ADVISORY COMMITTEE

Conducted Remotely via WebEx
Friday, April 30, 2021
10:00 a.m.

100 F Street NE
Washington, D.C.

PARTICIPANTS:

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HESTER M. PEIRCE, SEC Commissioner
ELAD L. ROISMAN, SEC Commissioner
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ALLISON HERREN LEE, SEC Commissioner
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P R O C E E D I N G S

MS. GARRETT: Good morning. I hereby call the April 30th, 2021, meeting, of the SEC's Small Business Capital Formation Advisory Committee to order. It is nice to see everyone again.

I also welcome the members of the public who have tuned in to watch the meeting via webcast on SEC.gov.

Julie, do we have a quorum for the meeting?

MS. DAVIS: Yes, we do. And I'll take this time to also give the staff disclaimer that anything said by the SEC staff today are our own views and do not necessarily reflect the views of the Commission, any of the Commissioners, or any of our colleagues on the staff of the Commission. Thanks.

MS. GARRETT: Thank you, Julie. We have two items on our agenda today. First, committee members will share observation on what we are preparing for and expecting with respect to capital formation and small businesses as we look ahead and begin to emerge from the COVID-19 pandemic.

Second, the committee will endeavor to build upon findings that we adopted last August encouraging the Commission to improve access to capital for underrepresented founders and investors.

Today, we will discuss whether there are potential changes to the securities laws that could help improve equitable access to capital via smaller funds since smaller funds often target smaller and underrepresented founders, including founders away from the coasts.

This morning, we are pleased to have with us Recently Conferred Chair Gary Gensler. He is here for opening remarks during his second week on the job. Chair Gensler, I understand that you are the child of a small business owner, as am I, which gives you a first-hand appreciation of the importance of small businesses.

Chair Gensler, congratulations on your new role, and we look forward to working with you. Would you like to announce some opening remarks?

CHAIRMAN GENSLER: Thank you so much. Yes. Good morning. Thank you, Chair Garrett, Vice Chair Solomon and all the committee members here today and the public tuning in on Webex. I know these are unusual times, but it’s good to have you with us as well.

I’m thrilled to meet the committee for the first time, and I look forward to the days when we can actually do this in person, God willing. And I’m honored.

This is my first advisory committee meeting, SEC advisory committee meeting. And I really do look forward to learning from this group, your debates, your counsel, your advice to the Commission. You're right to say my father, Sam Gensler, started and ran a small business in Baltimore, Maryland. Neither of my parents went to college. First generation Americans. So the committee's work really resonates with me.

And four siblings -- I can even go further. My mom worked in the business. Three of my older siblings went into the business, and it was a business that never had more than 30 employees.

A critical part of the SEC's mission is to facilitate capital formation. It's a three-part mission. But American entrepreneurs like my dad and those who are way more successful -- and my dad -- but American entrepreneurs and business owners rely on a wide array of sources to fund their companies.

That's one of the reasons that our capital markets are the envy of the world. Now, in my dad's case, what did he do? He used his mustering out pay from World War II. It was, like, 300 bucks. And he was an electrician. But he used to use the money, buy some vending machines, fix them up and then build what became a family business.

Now, today, who knows what -- what he would have done. He might have used equity crowdfunding platforms. But I think he would have needed my daughters or any one of his 10 grandkids to help him on that. And he was a little bit adverse to self-promotion. So might have been a little tough. But facilitating capital formation is so critical that it shouldn’t be about picking winners and losers.

And in the topics that you’re talking about here today is really so critical that all companies from small businesses to high growth startups and the like deserve access and inclusion in the capital markets. And it’s -- it’s really about the equal ability that a good idea can come to the capital markets and get funded or good management team, a good -- good user interface, good opportunities can access those capital markets regardless of race, gender, geography and other factors.

Now, as a society, we know this to be true, that we still have a lot of work to do to correct the unequal access to capital for underrepresented groups. My dad was never building a big business. But whether you’re building a small business or you have the idea for the next unicorn, the next potential billion-dollar market value company, it should be, regardless of your background, your belief system, everybody with a good idea and a good management team and a good entrepreneurial strategy should have those opportunities. I know this, that we all benefit from diversity and that our economy benefits from having this remarkable country of 330 million-plus, their ideas competing in the capital markets with a fair and equal access.

So today, I know you'll be taking this discussion up. You will also be talking about what you see in small businesses during these very trying times, the pandemic and -- and the COVID period. I'd also like to understand the intersection of these two topics, whether, during this 14 months, we've maybe potentially found more inequality and more stretching of -- instead of more inclusion.

And I think that if that's the case, we should look to what -- what policy levers within the authorities of the SEC that we have to kind of bring us back to a broader pass of inclusion for underrepresented groups in the capital markets for -- where a good idea can get funded regardless of -- of race, gender, color, ethnic background, sexual orientation, that everybody has a chance in these capital markets.

So I look forward to learning from your conversations about how to make the markets more inclusive as possible. This committee has a track record of agreeing with some of the actions of the SEC and some issues, saying, well, maybe there's an alternative approach. I like that. I like getting the good things, getting the debate going, hearing from advisory committees.

In closing, I just want to thank you all for representing the interests and ideas of small business owners, all small business owners across all communities. And you're helping us better understand how we can make them better for underrepresented communities and all communities in this country. Thank you. I turn it back to you and possibly other commissioners, I think, that are going to speak.

MS. GARRETT: Thank you, Chair Gensler. We look forward to working with you. We appreciate you being here with us today.

Today we also have with us Commissioners Peirce, Commissioner Roisman, and Commissioner Crenshaw. Commissioner Lee will join us after the lunch break.

Commissioner Peirce, would you like to make some remarks?

COMMISSIONER PEIRCE: Thanks, Carla, and thanks to the rest of the committee members. I look forward to today's discussion. Panels and discussions at prior committee meetings have helped me think about ways to ensure that capital is available to reach communities that have previously seen little capital flowing their way.

I think Chairman Gensler captured it perfectly when you said that no matter where an idea is, with whom an idea -- a good idea is, it should be able to get funded by our capital markets. I think that's a test of the efficacy of our capital markets.

But we've heard that most money comes from people within a founder's own community. And so we need both to empower and expand founders' communities by embracing technology and maintaining open mind. I'm going to keep my remarks brief.

I've mentioned most of these things before, but I continue to believe that the following items are part of the solutions, the problems that you're going to discuss today.

So first, I think we need to allow for greater flexibility in determining who is an accredited investor. An entrepreneur who's plugged into a network of financially sophisticated people should be able to go to those people for funding even if they're not wealthy enough to meet our financial threshold.

We need to open additional doors to accredited investor status such as educational credentials. We laid the groundwork for such an opening in our most recent accredited investor rulemaking, and now we need to act on it. And the Commission specifically invited this committee to make further recommendations including additional certifications, designations, or credentials that further the purpose of the accredited investor definition.

Second, we need to establish a framework for finders. That’s something that the Commission proposed last year. We received quite a number of comments. One of those comments explained that the proposal wouldn’t -- would, quote, enable less well-off entrepreneurs to raise capital more efficiently and -- and will, on balance, be good for society.

The Angel Capital Association observed that, quote, in some cases, finders can provide a specific role in facilitating capital formation for nascent, early-stage small businesses that often struggle to find cost-effective methods to raise funds beyond their immediate circle of family and friends, particularly in smaller, less urban locales where the density of accredited investors is limited.

Some other commenters were not as favorable, but many commenters, both for and against, suggested helpful changes. The third thing I think we need to do is create a streamlined micro-offering exemption. One of the refrains from prior meetings is that access to early money is really essential. And for many founders, a bank loan or dipping into personal savings are impossibilities. So a micro-offering exemption could allow an entrepreneur to raise 250,000 or 500,000 with only a simple notice filing, which would allow us, then, to monitor its use and then anti-fraud protection for investors.

I also understand that you will be discussing the qualifying venture capital fund exemption. Congress modified this exemption in 2018 so that now there can be 250 investors up from a hundred so long as other criteria are met. But this -- this exemption might be more useful if the fund could have more than the 10 million in assets currently permitted.

I look forward to your discussion of these and other options and for ensuring the capital goes where it can be put to good use. I think this will benefit not only the entrepreneurs who get it but also their communities and society at large. Thank you.

MS. GARRETT: Thank you, Commissioner Peirce.

Commissioner Roisman, would you like to say a few words?

COMMISSIONER ROISMAN: Absolutely. Just need to -- I think I managed the unmute. So good morning, everyone. Thank you, Carla. I'm pleased to see you all here, and I'm very much looking forward to your discussion today.

As the vaccine rollout continues, we are constantly assessing what areas of our economy need renewed focus. Given the disproportionate impact of the pandemic closures on small businesses and on small businesses owned by women and people of color, ongoing discussions about the needs of underrepresented founders are timely. Both today and over the coming months, I hope that this committee can help the Commission to understand the particular challenges these groups are facing.

I'd also welcome any recommendations you could offer for the SEC to ensure that our regulations and processes do not pose an unnecessary impediment to recovery. In that vein, I hope you'll take the opportunity to also explore how our rules related to perennial issues such as general solicitation, investment caps, and exemptions may disproportionately impact many of these founders.

I'm always struck by how deeply interwoven the different strands of our regulatory structure are. The knock-on effects of regulation in one area can have such profound and often entirely unintended consequences elsewhere. This committee has been instrumental in raising just these types of on-the-ground concerns, and we benefit enormously from your insights and discussions. To the extent that any of our regulations are imposing unneeded and unjust barriers, especially on groups that have traditionally faced barriers of all kinds, they fall well short of our mission and need our careful attention. I look forward to hearing your discussion, and thank you again for all of your hard work.

MS. GARRETT: Thank you, Commissioner Roisman.

Commissioner Crenshaw, would you like to say a few words?

COMMISSIONER CRENSHAW: Yeah. That would be great. Thanks, Carla, and thank you also, Jeff, and the rest of the committee for being here today and also welcome, Chair Gensler, to your first OASB meeting. It’s great to have you here.

And I just want to reiterate that I really agree with my fellow commissioners. You are tackling a critically important issue today, and that is what the Commission can and should be doing to promote more equitable capital markets. And I understand that later this morning, the staff of OASB will be sharing a video and some data that highlights how capital-raising experiences differ significantly depending on the gender or race of the founding team. It’s very troubling but not surprising to hear that women and minority-owned businesses face greater challenges when seeking and finding investors.

It’s very concerning to hear that investors who invest through funds seem to have more opportunities to invest with businesses owned and advised by White males as compared to those owned and advised by women and people of color. It’s imperative that the Commission examine the steps that it can take to promote greater equity in our financial markets.

This is a complex topic, and I really appreciate your willingness to work on these issues. And the last time we met, I indicated that I was particularly interested in hearing from you about the concrete steps the Commission could take to address the structural inequities and imbalances in our financial markets. So I’m looking forward to the discussion today, and I appreciate your -- that you’re willing to tackle it.

But specifically, I’m interested in how we could improve access to capital for historically underrepresented groups and how we can encourage broker-dealers, fund managers, and investment banks to facilitate offerings for women and minorities using their networks. And are there ways for the Commission to support institutional investors who want to allocate more investments to underrepresented founders? I'm interested in hearing your thoughts on these topics and other questions on your mind.

And finally, I know that in the past we've received feedback that changes to the accredited investor definition would be helpful in promoting equity. And while I appreciate and understand why this is a topic of interest, I do have concerns about whether it's the right approach. And specifically, I wonder whether underrepresented founders would be better served if we could identify and address systemic barriers of access to institutional funds and venture capital. Thank you very much for your time today, and I really look forward to hearing the discussion.

MS. GARRETT: Thank you, Commissioner Crenshaw, and thank you, Chair Gensler, and the rest of the commissioners. We appreciate your attendance today at today's meeting. So we'll move on to the first item on the agenda.

CHAIRMAN GENSLER: Can I just say one thing, Carla, and I know we're in a scripted sort of way, but I want to thank -- thank you for bringing this together because sometimes this is a way in the public under the government and Sunshine Act that our commissioners can hear from each other and talk to each other. This is not a Commission meeting. It's your meeting, but I thank you because it's really helpful to hear Hester and Elad and Caroline. I know that Allison -- we talk, and this is for the public as well. We talk bilaterally, one-on-one, and I've had more bilateral discussions in the last 10 days than you can imagine.

But it's sometimes helpful to just see each other all together. And so I -- I wanted to thank Hester, Elad, and Caroline for those because I think what I'm hearing is that we all share this goal, this -- this -- our capital markets aren't yet there. They're -- they've done a lot of really good things in the last 90 years, but they have not gone to the place where systemically anybody can access with a good idea the capital markets and that which Caroline mentioned about women and persons of color having less access to the capital markets.

So I just wanted to thank you and put a note that it's helpful to hear. We might have differences on the tools and the tactics, but we want to hear from you to solve this incredible important public agenda of the SEC. It’s right in our mission, fair, orderly, efficient markets. To me, I somehow read “fair” into this, also inclusion. And then capital formation is capital formation for all. Back to you.

MS. GARRETT: Thank you. I -- and we are honored to actually have all of you here today and Commissioner Lee will join us later. But it is -- it is a treat for our committee to get to hear from each of you and hear all of your thoughts.

COMMITTEE MEMBERS’ OUTLOOK: WHAT’S AHEAD FOR SMALL BUSINESS CAPITAL FORMATION?

MS. GARRETT: Okay. On to our first item on the agenda, which is -- you know, it’s been about 13 months since our committee had our first virtual meeting in response to the then new and extreme situation that small businesses were facing as a result of COVID. During that meeting, committee members shared observations from various areas of the marketplace and what they were seeing.

So today, we were going to have each committee member share observations of what you are preparing for and expecting in capital formation as we look ahead to hopefully emerging from the COVID-19 pandemic soon. I will call on each member to speak, more or less in alphabetical order.

We have a few changes because people have to leave. But if you guys can limit your thoughts to about two to three minutes so that we have sufficient time for every member to speak, I -- we would appreciate that.

And Kesha, you are first. Are you on the line?

MS. CASH: Yeah. Thank you. Good morning.

MS. GARRETT: Good morning.

MS. CASH: We’re focused as a venture capital fund on investing in companies that impact low- and moderate-income communities here in America, and that mission became more clear than ever last year due to the impacts of COVID-19 as well as the racial uprisings here in America. So we’ve been very much focused on racial equity through our investment approach and had a chance to witness the importance of safety nets in this country and access to upward mobility through our portfolio founders.

Our current portfolio we’re invested in, a number of companies -- some focus on financial access. One of our companies, Camino Financial, has been making small-dollar loans to Hispanic-owned businesses that otherwise would not get funding. These loan sizes are averaging $17,000, and we saw through the pandemic how important those dollars were and how resilient the community was.

Their loan default rates were much lower than the average, and they were able to work with their borrowers in a way that helped those small businesses stay afloat. So we're excited. They actually just recently received a CDFI designation. So we're seeing these worlds of FinTech and CDFI merge, bringing more technology, efficiency and hopefully scale to the CDFI community and working with community in a way that supports the recovery and the growth of small businesses. So we're super excited about that.

We're actually in reporting season as a firm and speaking to our own investors about what's next and how we want to allocate the remaining capital of our Fund II that we closed last year. And some of the things just quickly that our team is talking about -- and it's really at this intersection of racial equity, COVID recovery and then the brighter future that we're all striving for.

And some of these things are related to, you know, what we're seeing thankfully coming out of the Administration around the stimulus bills and different acts that are being passed. So there's a -- a $10 billion carveout, as we know, for Black farmers focusing on regenerative farming and other ways to grow on that land to create economic opportunity. That's really exciting when you think about the green economy and agriculture. We're also doubling down on investing in technologies focused on women, women in the workforce and what COVID taught us and showed us. What does that mean for working women and moms?

And a third thing we're excited about is fractional ownership. How do you democratize access and ownership when we think about people staying in their communities and being able to own in their communities? So really excited to be here to have this conversation and looking forward to hearing from others. Thank you.

MS. GARRETT: Thank you very much, Kesha.

Greg Dean?

MR. DEAN: Hi, Carla. Thank you for having us here today. And FINRA does thank you and Martha for inviting us to be part of this in a nonvoting capacity as advisor to the Capital Formation Advisory Committee. We very much appreciate that.

Since last year, as you know, FINRA has been quite active in the remote office space with both ourselves internally as well as overseeing our member programs that are also in a remote -- in customer interactions as well as in trading. With regard to the post-COVID and getting back into the office, what FINRA has done is, at the end of last year, we issued a regulatory note asking for comments.

FINRA sees comments and lessons learned from the COVID-19 pandemic. We’ve also been working with our advisory committees on what rules or guidance may need to be changed and working with the SEC on how to implement those.

We are still taking comments, and if there are any good ideas/suggestions that we need to do, both from broker-dealer stance or from investor stance, we would welcome those. In addition, with regard to the topic later today on underrepresented founders and investors, as you all know, a few years ago, FINRA did establish the securities industry essentials exam which allows people to take the exam without having to be associated with a broker-dealer, which has broadly widened the availability for people to enter the securities industry.

We’ve also taken a number of steps in recent days. Last fall, we established a racial justice task force looking at how FINRA can improve ourselves as well as working with our member firms in the racial justice task force area as well as third-party stakeholders, investors and so forth.

And yesterday, we took another step in this. We issued a regulatory comment which FINRA seeks comment on supporting diversity/inclusion in the BD industry. So we specifically are requesting comment on any aspects of our rules, operations and administrative processes that may create unintended barriers to greater diversity and inclusion in the broker-dealer industry or that might have unintended disparate impacts on those within the industry.

So we have this comment period open until the end of June. This is clearly so important for us and the industry as a whole, making sure that if there are anything that is unintended in our rule set or guidance or application, we want to hear about it. And we will work closely with those within the industry to make sure how we can make changes to meet and improve the situation.

In addition, the FINRA Foundation recently introduced -- worked on new research with the NORC Foundation of the University of Chicago looking at investing in 2020, new accounts and the people who open them, which is really groundbreaking research that has not been looked at before.

We did a survey back in November of new investors and some experienced investors and how they interact with the marketplace. One of the most impressive things about this is we did a breakdown by demographics looking at the different demographics of investors, how they receive information and how they interact with the marketplace.

We're also going to be continuing this research on with follow-on studies in the coming year. One of the most surprising aspects of this is we did look at those new investors that use apps to trade online. And about 56 percent said they did. And those that did use trading apps traded between one and three times per month.

So this is groundbreaking research. We look forward to working with the Small Business Capital Formation Advisory Committee and others that are interested in this area. Thank you.

MS. GARRETT: Thank you, Greg. We appreciate your thoughts and thank you for being here as a member of our committee, and we appreciate what FINRA is doing. And the next person would be Jason Seats.

MR. SEATS: Howdy.

MS. GARRETT: You available?

MR. SEATS: Sure. I'm here. So I'll have a couple comments. The main trend that I'm curious to see how it plays out is this thing that we're doing right now, which is virtual meetings and how does that change. And I mean, it’s had a lot of impacts on capital formation and fundraising. Obviously COVID accelerated a lot of market trends in venture. And that was a boon and is a boon to many startups and investors.

And in many respects, venture as a whole, venture capital, was business as usual, got back to business as usual by mid-year last year. We, as a firm at Techstars, were out fundraising over the last year. So I was in market fundraising entirely virtually starting in Q2 for a fund that we closed in Q1 of this year so got to see that firsthand, both on the deployment side for us but in the fundraising side.

And I would say other than specifically Q2 of last year, there really was no slowdown in the flow of money going into venture capital funds and from funds themselves into startups. But the -- a trend that was a pre-existing trend has accelerated and is still evident, which is that the most desired, coveted, hyped growth stage venture companies can raise money very easily. And others have a harder time.

And so there’s becoming a bit of a have and have not on who can raise money and how easy it is for you to do, both at the firm level for venture firms but also at the start-up level. And my sort of narrative on why that's the case has to do with this, with virtual. And sort of venture -- venture is equivalent of flight to safety in the uncertain times and when there is an increased cost in making new relationships. And so when you have to source investments and you can't meet people in person, it's harder to get to the level of comfort that you would otherwise get to, to make an investment. And I think the net effect of that is it caused a lot of intro investors to do something they were already doing anyway, which is sourcing through their personal networks but to double down on that really deeply.

And that had, I think, a net effect of making it harder for sort of the outs crowd to be able to access that capital as obvious touchpoints to underrepresented and underestimated founders and their ability to raise money. And so my -- I don't know that I have a prediction on this, but my curiosity, the thing I'm watching for, is what -- how -- what is going to be our desire to meet in person again after all this is done, and how quickly is that going to happen?

Pretty early on, people were happy to call the trend that virtual remote work is maybe the future, and maybe we -- no one needs offices anymore or whatever. And you -- a couple quarters go by and -- and now I'm feeling that humans are just craving this actual physical contact with each other. Maybe the persistence of the virtual remote won't be as big as it was in the past. But I do think it has a lot of impacts on -- again, on new network -- you know, people being -- access new networks for capital raising.

MS. GARRETT: Thank you, Jason. Those are some interesting points, especially about the working virtually and the effect that it could have on fundraising.

Greg?

MR. YADLEY: Thank you. Welcome to our new chairman and all the commissioners. Thank you for being here today. We're seeing that innovation matters. With all the disruption to supply chains, economic dislocations that resulted from the pandemic and shutdowns and starting up, companies that have been able to adapt were the ones that have been successful. Resourcefulness has really mattered.

Capitalizing on new behaviors and trends, those companies were getting funded, pivoting to virtual relationships. Learning to operate more efficiently with lower expenses has focused a lot of companies, and those lessons, picking up on what Jason just said, to a greater or lesser extent, are going to remain part of the strategy going forward.

Since most of my colleagues on the committee will respond to raising capital directly, as Carla asked, through securities offerings, I wanted to comment on another aspect of small business growth, one that's providing a lot of capital to smaller businesses indirectly at a higher level. And as significant as any individual company's profile is, what I see is the environment, which has not fundamentally changed since early 2020. In terms of capital for growing businesses, for many, funding opportunities have been overshadowed by opportunities to sell or recapitalize. Public companies are looking for scale and growth. Private equity firms and SPACs are looking to invest capital.

Valuations are high. Cost of capital is low. And as two more speakers have already said, new funds are being formed, and so the competition for good companies is intense. So in the lower middle market, this has led to truly robust M&A activity. And buyers are asking the questions they always ask; right? Who has a concept or a niche perspective that can create exponential change?

Who has a track record that is sustainable going forward? Who has embraced technology that will straddle the old economy and the new economy? Who can generate cash flow, and who can scale rapidly? Lots of things are driving this, the demographics of aging business owners, concern about higher tax rates. But a lot of it is simply private equity that last year was more than a quarter of all M&A activity, the highest proportion since before the global financial crisis.

I saw a report that said at the end of last year, financial sponsors are on $2.9 trillion of available capital to deploy. At our law firm, we're seeing M&A interest at almost every sector, healthcare, manufacturing, tech, B2B administrative and processing services.

And SPACs have definitely fueled more interest in operating as a public company. Our committee has talked about some of the costs and regulation that may be reasons why companies continue to prefer to stay private. But companies now see SPACs as a viable option to successive stages of M&A. So those were my comments, and I look forward to hearing other people's views and experiences. Thank you.

MS. GARRETT: Thank you, Greg.

CHAIRMAN GENSLER: Carla, I don't know your call to order, but on the SPAC issue, are they seeing it viable -- why are they seeing it -- you used the word "viable." Are they seeing it viable, or are they seeing it sort of preferable? Is there some regulatory or legal or other arbitrage going on? I know you've got a tight agenda with a sort of one- to three-minute answer.

MR. YADLEY: Yeah. Well, because that's -- as you know as well as anyone from an academic and a regulatory perspective, those are key questions. But for a lot of smaller companies, one of the things that we counsel them about is a good buyer is a buyer who can close in addition to everything else, the price -- right? -- the culture, all those things. Can this person close? And SPACs are -- they're sitting on money. They have time pressure to deploy it. And I think that's an element.

That's a little bit, Mr. Chairman, a superficial answer, but for an average business owner, some of those more complex issues, they're not front of mind. And we've decided to sell, and here is somebody who's got money.

CHAIRMAN GENSLER: Got it. So, no, it was a -- it was a good -- I understand your answer. You're saying timeliness and certainty of closing.

MR. YADLEY: Right.

MR. SOLOMON: Yeah. I would also say, though, not to interrupt but Chair -- Chairman Gensler, I think for the most part, SPACs at the larger size are the companies we're talking about here. So when we're talking about this group, generally we're talking companies that have a much smaller market capitalization.

And for the most part, SPACs are not really appropriate or inaccessible for companies that are under $250 million in private market capitalization. So I think a lot of conversations that are happening are about when they grow -- when they get to be bigger companies, are SPACs appropriate ways for them to access public market capital?

CHAIRMAN GENSLER: Right. I was just tapping into a -- you know, but I appreciate, Jeff, that it's really not something that's much in the small business and capital formation side, but I was intrigued to even hear it come up. So thank you.

MS. GARRETT: Okay. Thank you, Greg, and thank you, Chair Gensler, for your question. Feel free to obviously ask any questions. I am next.

And so I'm a corporate lawyer at a law firm. And, you know, I tapped into some of my other lawyers in my firm to see what people were seeing. And it was pretty overwhelming. Everyone is like, oh, there's so much capital to be deployed. You know, there -- people are going crazy with fundings and all different rounds of capital formation.

And also, people were talking about, of course, the very active M&A market that's going on right now. And so I found it very interesting because I also, though, heard and I have familiarity with small businesses that aren't the lucky ones to be able to tap into those markets and are not the recipients of the capital and are having a harder time getting capital.

I, as a lawyer, don't know the difference between what is making some companies be able to get the capital and some not. But I would imagine some of the things that we're going to address later on today may be some of the reasons. But so I wanted to speak a little bit about the small businesses that might not be the recipient of the capital and the M&A transactions right now.

What I'm seeing with those small businesses is that even though we're emerging hopefully from COVID, you know, COVID has had a long-term impact on these companies. If they've been able to survive during the pandemic, then they have most likely used up a lot of their cash reserves. They probably have some of their, you know -- their big cash payments that they had -- you know, were making.

Maybe the -- were on hold as a courtesy during the COVID pandemic such as loan payments and lease payments. And so therefore now, they're starting to have to expand their cash again. And as a result, the companies are becoming very pressed. And so even though we're getting to be on the other side of the pandemic, many of these companies are very low on cash. They've, you know, been able to get as much PPP loans as they can.

And now they're hoping to see if they can survive post-COVID. And obviously during the COVID pandemic, they were not investing in their infrastructure, in their companies and their hiring as much as they probably wanted to. And therefore, it's going to be harder for them to be able to get revenues back up to pre-COVID days.

So I think a lot of people are thinking that if we emerge from COVID and you're a small business and that you've survived, then all's well and fine. But what I think is that there's going to be a lot of small businesses that still really need to have access to capital. And I know capital is flowing into a lot of different places, but it's not flowing everywhere. So that's just my takeaway from where we are in the pandemic. And thank you. And the next person is Sara.

MS. HANKS: Thanks. Thanks, Carla. Yeah. I wanted to echo some of the things that Jason had said because really we’re not seeing COVID -- apart from the fact that COVID has had the impact on the small businesses that you mentioned, Carla, from the point of view of the online capital formation world, really I’m not anticipating a difference post- the post-COVID world from COVID itself. The real big difference was the impact of COVID itself. In the very early days of the -- of the pandemic, there was a lot of panic, and we thought, my goodness, what’s going to happen?

The amount of money invested in the various exemptions, regs here, for Reg D, Reg A, increased hugely. I mean, we saw exponential growth. And in some ways, the online capital formation world, the crowdfunding world, is a perfect COVID business. We would, you know, anticipate this to continue now that people have got used to it and to see further growth in the changes due to the growth in the business due to the regulatory changes that went into effect last month.

As Greg had talked about, there are new investors in this market. And I think this is a very important development. You’re seeing younger investors coming in, looking to support various businesses. To me, I think it’s still -- we need to look at the demographics of that new cadre of investors. It does seem that it’s coastal. It’s male. It’s younger. And these are investments that everybody could make under certain circumstances.

And then I have a request rather than a prediction. With all of these changes and with all of this growth, there is a need for guidance from the staff. I want to shout out to the Office of Small Business Policy and to the Advocate's Office, who have been incredibly helpful, fast, and responsive in providing answers to questions for -- you know, with respect to rules that just went into effect days ago. And they've been tremendously helpful.

I would like there to be a way for guidance to be disseminated faster and more broadly because just Sara, you know, talking to the office and then telling our various clients this is how it should be, that's not enough. I mean, we need to have definitive answers on a website, even if they are not definitive final answers. And that would include guidance on the application of the new rules, compliance and disclosure interpretations or some other Q&A format and also I -- we are begging for guidance on the circumstances in which online platforms who are not broker-dealers are subject to broker-dealer registration. So really hoping that that will -- that is something that the Commission can help with. Thanks.

MS. GARRETT: Thank you, Sara.

Youngro?

MR. LEE: Yes, thank you. So the last 12 months plus has been really an incredible period for -- in good and bad ways for small businesses. And my role as founder/CEO of NextSeed, which is an investment crowdfunding platform that focused primarily on, really, small businesses and even in the industry, there has been changes where I’m now also associated with Republic, which is another investment platform that focuses on more tech companies.

And it is absolutely true, and I cannot emphasize enough. There is hundred percent a massive divergence in the type of companies that we’re talking about. Anything that’s tech-related companies, anything that is high growth has absolutely been -- I mean, it’s been the best years ever ironically, and we see that in the stock market as well.

On the flipside, as Carla mentioned, in the small business space and what -- by this, I’m not talking about any -- under $250 million. I’m really talking about businesses that are trying to get $250,000 in annual revenues. It has been decimated. And there is no getting around that.

We see the stats as well, the type of

companies that are raising capital. And this is a -- I'll say the bad stuff, but I'll end with a good note. The bad stuff is these small businesses that are trying to survive, literally survive -- nothing else -- survive -- they were -- they did not have access to capital during this period. Definitely the government loans were amazing.

As we all know, that is not enough. And as a result, a lot of businesses did shut down. The silver lining, if you will -- and we know this from our own experiences. Even on the businesses that we help with on NextSeed, probably less than 10 percent of the businesses actually went out of business. The vast majority of them survived, in my opinion, precisely because of the fact that they utilized, and they had a community behind them in the form of investment crowdfunding.

So many of them actually renegotiated. We helped them renegotiate their campaigns, their notes, and the investors. Hundred percent, almost everyone, like, either forgave or allowed -- give flexibilities on different payment obligations. And as a result, this is strange to say. But in 2020, through our platform, small businesses actually paid back more than they ever did in the previous years.

And it’s because they were able to get through the really crazy months of the summertime especially. And when things got better when they were able to get the loans which -- and so delayed, and they were able to, you know, get back on track, they -- the business owners themselves then were able to, you know, do what they could to make up for the losses, including payments to investors.

And this is a very psychological thing that I really want to emphasize both now and hopefully the future, is to be able to understand these are people involved. So small business owners, they want to do the right thing, and they really want to do the right thing for themselves and their communities and their families.

I know one of the commissioners mentioned about the idea of allowing a bigger systematic path for institutional and VC investors to invest. What I can actually say from seven years’ experience is institutional and VC investors are not systematically designed to support the local, smallest businesses. So if we really want to encourage and support the small businesses under -- at the local level, we have to allow access to more individual investors who might not be at that level to support the local businesses.

And having said that, the final note that I will say is the new rules that SEC did generate, especially with the support of this committee, has been absolutely, absolutely amazing. And that is the number one example of how the government and community and private sector would come together because, as a result of that, I know for a fact several businesses, using the Reg CF exemptions for COVID, would -- are alive today, and they would hundred percent not be alive had they not been able to use -- utilize those rules.

The new rules that increase the limits are also -- different owners. A couple of our business owners -- businesses that raise capital, including Backstage Capital. And it's a Black woman-owned business as well as another company that is also owned by a woman for a woman's sexual wellness industry.

These businesses are absolutely utilizing the new rules and raising capital that they would, in my mind, not be able to do. So really want to appreciate the SEC for -- despite the difficult times committing and making those changes. Thank you.

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

Sapna?

MS. MEHTA: Hi, everyone. Just to give you -- I'll try to keep this brief so we can stay on schedule.

But, you know, my observations from the Rise of the Rest Fund, which is part of Revolution, we have made it our mission to invest, you know, in areas, in cities outside of New York, Silicon Valley, and Boston. And we’ve really doubled down on that this past year. I mean, I agree with Jason. Other than I -- you know, when -- when COVID first hit and we were more in, you know, lockdown mode, I think investment activity and valuations have just skyrocketed this past year. You know, we -- after the George Floyd death last year, we sort of scratched our heads and tried to think of what we could do, you know, in order to not only spread out capital throughout the country but among minorities and women.

And instead of our regular bus tour that we do, we decided to do something called an equity addition tour where we had pitch -- the pitch competition applicants had to identify as a minority for Black or Hispanic founders. And we got Morgan Stanley to coinvest along with us and OHA out of Atlanta.

And we’ve invested probably -- you know, we do smaller checks, but we’ve invested a little over a million and a half in those winners and we -- runners up. You know, what we have found, our fund -- we make diversity a priority so about -- I don’t know what the current numbers are, but it’s usually around 35 percent of our investments are in minority founders.

And we’d like to continue that trend. What we have found is that it has been very hard for younger fund managers. So we invest in operating companies, you know, as we take advantage of a venture capital exemption. But we have seen some struggles from younger, diverse managers taking longer to be able to raise their funds. We’ve done small checks to some of them, but we are obviously hamstrung by the 20 percent requirement or restriction that we can invest in funds.

But we would obviously like to see that increased because we think that sort of makes everything go round. It’s all part of the same ecosystem. But, yeah, I mean, other than that, I think this year has -- we’ve just seen an explosion of, you know, new rounds, valuations. And, you know, as majority of our companies are tech companies like Youngro was pointing out the distinction, they have been doing fairly well here. That’s it.

MS. GARRETT: Thank you very much, Sapna. We’re going to move on to Mike.

MR. PLECIAK: Hi, Carla. Thank you very much.

MS. GARRETT: Hi, Mike.

MR. PLECIAK: And thank you very much for accommodating my time, and it’s great to see everyone and I’ll -- my friends from the committee. And I’m glad to be back representing state regulators on the committee. So I thought maybe I’d just tell just briefly the experience that we’ve had in Vermont, and parts of our experience, I think, are representative of the country as a whole. So I think everyone knows that, you know, obviously COVID impacted minorities and women to a greater degree when you look at sort of the health and economic statistics.

Just here in Vermont, you know, our unemployment roles -- you know, 54 up to 73 percent of those getting unemployment on a regular basis are women. We’ve seen more women impacted in terms of workforce and having to leave the workforce for a variety of reasons during the pandemic. And, you know, during the previous recession, I think that was the inverse, that men were more likely to be unemployed after 2010.

So what does that mean for long-term -- the long-term impact in our state? And again, we’re not unique. I think this is something that’s happened across the country. You look at the businesses in Vermont that are impacted, retail, hospitality, restaurants. Our ski resorts lost, you know, over a hundred million dollars, it’s reported, this ski season.

So I think all of that sort of boils down to, you know, the change in human behavior that we are seeing and whether that's a long-term change or a short-term change. So how quickly will people feel comfortable traveling to go skiing? How quickly will people feel comfortable having business trips? We have plenty of businesses that decide having their business trips in Vermont -- you know, how will human behavior revert back to being willing to shop for certain products on Main Street rather than seeking those products online? How does that impact retail? Even things like Vermont's population, we saw dramatic increase in out-of-state homebuyers during the pandemic, an increase, you know, 40, 50, 60 percent compared to 2019.

So we've seen more people even moving into our state. So I think how all of that lands and works itself out is really putting some of the investments sort of on hold as people wait to see, again, you know, how have these behaviors changed for the permanent, and how have they changed, you know, just during COVID or temporarily?

From the lending side, you know, we have -- we see our banks are very well-capitalized. Their deposits have gone up over 20 percent during the pandemic.

Again, I think that’s representative of the rest of the country. You know, some of that’s driven by PPP loans being put into deposit. Some of it’s driven by people not being able to spend their money in the same way, you know, during the pandemic.

So at least our experience is that there is plenty of capital for lending, you know, through sort of commercial lending opportunities in our state. And then the last thing, I’ll mention that -- is an initiative under the American Rescue Plan that we’re excited about in Vermont. And this is the same in every single state. But there is the State Small Business Credit Initiative under the American Rescue Plan that sets aside about $10 billion to states.

And this was a program that was first enacted under the JOBS Act. And I know Vermont took advantage of that and created a lending program. But it does not have to be only lending. It can also be equity investment as well. And I know just for our state, we’re anticipated to get four times the amount of money that we received under the JOBS Act.

So we’re very interested in Vermont and trying to understand how we can create opportunities to invest equity investments in small businesses and have the state be a facilitator in that. And again, that’s a program that’s available to all states across the country. So that’s one thing that we’re -- we’re keeping an eye on. And with that, I’ll -- I’ll leave it there, Carla.

MS. GARRETT: Thank you, Mike. And we welcome you back to the committee again. And we appreciate your point of view from what is going on at that state level so thank you. Martha?

MS. LEGG MILLER: Yes. And welcome back, Mike. Glad to have you back on the committee. So I’ll be very brief because I think many of you know a lot of what we’re looking at because we published a report to Congress telling Congress exactly what we’ve been seeing with respect to not only COVID trends but broader macro trends.

Some really bright spots. There’s a lot more companies looking to join our public markets. There are signs that there’s a lot of entrepreneurial activity underway and new businesses being formed, both opportunity entrepreneurs, people that are proactively seeking it out as well as necessity entrepreneurs, people that realize that is the path that is available for them.

And there’s a lot of thoughtful engagement that we are seeing and welcoming on supporting underrepresented and underestimated founders. A couple of troubling trends that we are very focused on understanding. One is a decline in those first-time and smaller funds. We have seen the data showing that, yes, average activity shows that there has been a lot of money pouring into funds that are focused on private market investments. But those tend to be larger dollar amounts and in larger funds, and it is skewing what is happening at the bottom end. As Sapna was mentioning, it’s taking longer for those who are looking to bring together a smaller fund to actually find investments and close on it.

Another trend that we have seen is that there’s a lot of investment going into later stage and tech and high-growth companies, which I think everybody has acknowledged here, so we’ll just reiterate that we’re seeing that. And funds are doubling down on their existing portfolio companies to make sure that they come out of this intact.

And what that means is it’s a lot harder to raise first-time capital and smaller dollar amounts, particularly when you would be looking to be a very small proverbial fish within a big pond of a large fund. So that is -- those are some trends that I think will have dramatic impacts when we’re looking outside of hubs where capital-raising activity is really coming well, and we’re looking at the rest of the country as well as ecosystems that may have more entrepreneurs who bring diverse perspectives that aren’t as well-represented in our capital markets. So looking forward to the committee’s ideas on ways that we can work to address some of those issues. Thank you.

MS. GARRETT: Thank you, Martha. And we will be talking about that in our next agenda item.

Catherine?

MS. MOTT: Thank you, Carla. My perspective is going to be focused on what I have seen here in the Midwest. For us here, that, you know, in Pittsburgh, we -- we’re located in Pittsburgh, but we invest across through to Chicago. We’re a small fund, a micro-VC fund, and a, you know, professionally managed angel investor network.

I’ve been doing this for 19 years. My sense of things are that what I have seen in the market has only been amplified by the pandemic. We all know that 76 percent of the capital is -- venture capital is on the coast. The Midwest remains an underserved market. And I’ve heard it addressed by a couple of others today.

Even though we have great IP and universities and we have multiple angel groups, we have solitary angel investors, micro-VC funds, crowd funders, incubators -- accelerators have their own seed fund. Plenty of seed funding, I -- we’ve continued to see at work in our region. But the Valley of Death for our region is the lack of Series A funding. That’s at a point where, after seed funding, the company has exhibited proof in the market. But it needs capital to scale. And in this industry, it’s called cross the chasm. That’s a point where a company needs 3- to 10 million. And keep in mind, they are still not bankable.

These companies still probably are not cash-flow breakeven. The fund size that serves that market is the 50- to $150 million. The stumbling block here is the 99 investor rule. I live in this space. This is the space that we seek often follow-on funding. There are plenty of investors. So let me talk about the group. I live in the accredited investor world. And as former chairman of the Angel Capital Association, I know this market well.

There are plenty of investor groups -- as a matter of fact, ours is one of them -- that can raise and have raised the $25 million fund. That’s because we can tap people who are willing to invest 250K over 10 years or even 100K over 10 years.

But the problem is we can’t get to that 50- to

150 million number that would be a very viable Series A fund. If we, you know -- so having said that, what -- what would Series A funds do? They would do one of three things. They would bridge the company to a Series B where they can, you know, attract coastal interest because coastal VCs aren’t going to come into the market unless they can deploy 20- to 30 million from their fund and syndicate with three of their partners. So a Series A would bridge to the Series B.

Secondly, it could also provide a viable opportunity for a strategic acquire to acquire the company. Everybody gets a chance to have a profitable exit. And that money gets deployed back into the market. Angel investors will continue to recycle and so will VCs.

And it could also get the company to cash-flow breakeven and then become bankable. I will say this. I have been invited to the Texas teachers’ event and the Grosvenor event, and I have talked to multiple institutional investors. And even yesterday, I talked to a fund of funds.

Their minimum is typically 15- to 20 million that they can invest in a fund. And that is also -- you know, they are not going to expose themselves, you know, to being any larger than 10 percent of any fund. So when you ask them for money, they are not going to invest in a 50- to $150 million fund that can serve the Series A round need for many start-up companies.

It continues to be a problem in the Midwest. My concern is, you know, all of us who have been in the market have done exactly what everybody has been talking about. We have extended the runway for our companies. We have supported them through the pandemic. But what is not changing is the need to fill that gap that has become the Series -- what we're calling the Valley of Death. Thank you.

MS. GARRETT: Thank you, Catherine, and I hope we can address some of these issues later this afternoon, this morning.

Marc?

MR. SHARMA: Thank you, Carla, and good morning, everyone. I just have a brief update from the SEC's Investor Advisory Committee. Some of you may know that last month the Investor Advisory Committee issued recommendations on minority and underserved inclusion in investments and financial services.

Those recommendations are available on the IAC website on SEC.gov, or if any of the members is interested in getting a copy, I'll be happy to share those recommendations with you. Just ding me. That's all I have. I'm eager to hear from our fellow members who are on the front lines. So I yield my time back to you, Carla. Thank you.

MS. GARRETT: Thank you, Marc.

Jeff?

MR. SOLOMON: Thanks, Carla, and thanks to the commissioners for attending today. It's always great to have that support. I'll just start with a shameless promotion for the Office of Small Business. It's a true gem of the SEC. I've spent a lot of time working with a number of different parts of the SEC, and what the staff do in this area is really phenomenal and thoughtful. And so again, I just feel lucky to be a part of this because it -- the work that we're doing here actually has the opportunity to impact lives and for many, many generations to come.

As a -- also a -- the child of a small business owner in Pittsburgh, Catherine, as you know, you know, this is near and dear to me and is very personal because I watched the ups and downs and sideways and the difficulty that my father and mother had securing capital and the fact that they had to mortgage everything just to have enough money to actually get the business to run.

And, you know, did that for 38 years and able to put two kids through college. And so I wouldn’t be here today if it weren’t for their efforts and their willingness to take risk. And so for me, this is a work of passion. We absolutely need to be looking at ways to open up the spigot for capital formation for small businesses but also open up ways for investors to participate more in wealth creation. I think the thing that I’ve noticed over the past year is that we’re still working out investor protection and capital formation. These are two sides to the same coin, and we have to be very careful as we think about how we -- we bridge that gap.

We’ve certainly seen in some instances, particularly with the advent and the public markets of -- of fractional share ownership and things like that where we’re getting a lot more participation from individuals in the market than we ever have before. I view that as a positive. But I also think along with that comes the attendant risks associated with having individual investors maybe not as well-informed as they should be.

So I think we need to think about ways to do -- not only educate companies on how to access capital but also investors. And I think financial literacy has to be a big part of what we do echoing sort of some of the things that Marc just talked about, working very closely with the Investor Advisory Committee on how to do that so that we can help the SEC and the staff to meet the objectives that -- of capital formation, fair and equitable markets, as well as investor protection.

So to me, this has been a big -- the big change that I've seen over the past year is that there are more companies getting access to the public markets. And there seems to be an increased amount of companies that want to get access to the public markets.

And while a lot of the companies that we do business with in Cowen where we focus primarily on the institutional market so not really dealing with individual investors, what we see is that there are more companies from all across the country, not just at the coast, who want to get access to capital and that coastal capital is more likely to invest in the middle of the country when it sees opportunity to have liquidity at the back end.

And so a number of transactions that we've had, whether it's been in private investments or SPAC, back-end mergers or things like that, when the public markets and when the venture capital -- when the public markets are open, venture capitalists, the kind which Catherine was talking about, and public market investors, which is ultimately where a lot of the capital comes from, are willing to make investments in earlier stage companies if they believe that there will be liquidity at some point in the not-too-distant future. So making sure that we have the access to capital markets is going to be a really critical thing as the trickle down will occur. And even though we may be talking largely about companies that are larger than the $250 million minimum -- the $250 million market capitalization size, knowing what's happening just above that is really an important way because that provides the liquidity and the exit that a lot of investors want. The investors, they'll be investing in the companies that we're talking about maybe. And it also provides tremendous liquidity for individual investors who will be investing.

So a year after this all started, the big takeaway for me is more companies than ever want to figure out how to get access to the public markets. And if we can do that particularly at the smaller level, we can create significant amount of jobs because we do see that when companies access public markets, they do create more jobs, and that's a great thing for us to be doing in this time.

And I would also say, you know, when I look at the great things that have happened in the public markets over the last year since -- over the last 10 years since the JOBS Act was actually passed in 2012, certainly we've seen biotechnology continue to access that, and I don't think it's -- I don't think it's a stretch to say that we would not have vaccines today if it weren't for the public markets in the United States of America because Moderna and BioNTech would not have been able to get the capital that they needed in order to have the technology ready to go. And so if you need justification for why we need healthy markets and all of the things that are really critical, look no further than that. It's a miracle. And the capital markets in the United States and the efforts that many at the SEC made and Congress's foresight on the JOBS Act are a critical reason why we are where we are.

And as we think about the things we need to do to improve it, we should just take a moment to at least be thankful that we have the best capital markets in the world and that they do some great things for people at their moment of greatest need.

MS. GARRETT: Thank you, Jeff. Appreciate those comments.

Hank?

MR. TORBERT: Hi. How are you all? This is

Hank Torbert from AltaMax. First of all, I want to thank both the commissioners as well as all of my committee members. I know it’s been a while.

I’d like to start off by saying -- reminding everyone that small businesses are the lifeblood of this country. And we must always remember that no matter what we do. As many of you know, I run a manufacturing operation in the Gulf Coast. And I’ve seen some very interesting trends, and I’ll break them down into financial, operational, and then also new innovation, if you will, and technology.

From a financial standpoint, what I’ve observed is over the last year, clearly there is a need for capital formation support for small businesses clearly. There are many businesses that were strained or could not operate. Supply chains were significantly held back, damaged, or delayed, hurting several of our companies throughout our region and others.

What I saw for many of the larger banks as well as some of the investors -- and some of you may agree -- there was a flight to safety, if you will, in terms of focusing on known businesses or easily understood businesses resulting, in some cases, for a -- for smaller business to seek out innovative financing or innovative structures and the like.

Even ourselves, we did something along those lines. From an operational standpoint, as I said before, supply chains are clearly strained. And there's been a significant focus on operational strength as well as managing your business as -- as thinly as you could or, if you will, managing your business as leanly, if you will, because it's been a rough 18 months for, I think, many small businesses. And then lastly, what I've observed is the focus on innovation. I think, quite frankly, given everything that's happened, many companies, notably in the industrial space, have focused on any sort of innovations that could help them operate more efficiently. And that's something we've never seen before, but even businesses of our size are doing the exact same. So those are my three observations.

MS. GARRETT: Thank you, Hank. And it's nice to see you. Thanks for joining us today.

MR. TORBERT: Sure.

MS. GARRETT: Sue? Hi, Sue.

MS. WASHER: Just needed to unmute myself. So thank you for having me here today, and I really appreciate being part of this group. And I really echo many of the things that previous members have stated. And I want to specifically say that I'm very supportive of the expansion of the definition of "accredited investors." I think, especially in the life sciences where my company resides, you know, the hardest money to get is the first money.

And so having the ability to really expand that friends and family group to include MDs, Ph.D.'s, people that can then help vet your technology to later stage investors I think is critically important. Also, I would -- I agree with Catherine that the -- the 99-person limit can really hurt the ability to form those Series A funds, which I do believe are just critically important.

They supplement things that are working such as the SBIR, the STTR programs, and NIH grants. But I think that those Series A funds are very important. I think that kind of -- you know, our company has moved from that stage. We are publicly traded. And I think one thing I would point out, that in the life sciences, I think a lot of companies that this committee and others would consider to be very large because of their market cap are really, truly still very small companies with a burden of reporting that can be onerous because we have larger market caps because of the research engine, and where our funds really need to be spent is on like things that Moderna was able to do to develop a vaccine.

And so we spend our money on the science and the research. And sometimes, some of the 404(b) requirements, the quarterly reporting for a development firm who has not -- is not revenue-based, reporting every quarter sometimes does not make sense and is not a good use of the company's resources. I think that's very important to understand. And also, investor transparency is very important to biotech companies and life science companies. I think many of us are somewhat concerned about the increase in retail involvement in early-stage biotech companies. We don't know how to interact with them.

We don't know how to explain our science. We don't know how to know who they are that are investing in our company. And many times, they really don't understand the very technical scientific information that we release. And this is a big concern of us that has grown over the last year.

The other thing that I will say is that one of the biggest impacts on anyone in the life sciences that is not working on COVID -- and I would make the argument that we need to continue to work on a wide variety of things for the health of our country and the world -- is supplies. There are many, many supplies within the biotech industry that are seriously constrained at this time.

And many smaller companies have no leverage over vendors or manufacturers and were last in line to get critical supplies that we need to do the experiments, to develop the new products that are going to benefit patients. And so this is something we're very, very concerned about. Also, the other issue that is a big concern is that, as others have pointed out, there have been a lot of companies that have gotten access to the public markets, especially in the -- in the biotech and life sciences space. But what we have found is that there is starting to be a very critical shortage of experienced personnel.

And there is a lot of competition for people that truly have the experience to be managers, directors, supervisors, executives within these companies. And that is -- and this touches on immigration policy a little bit. And we have to understand that.

Now, some things that I've seen done that I'm very hopeful for is that two organizations I am a member of, the bio industry organization as well as the Alliance for Regenerative Medicine, have really taken on this issue of trying to develop the next generation workforce. At ARM, they have formed at the organization’s expense a internship opportunity for minority students in STEM, regulatory affairs, and law and are really sponsoring these kids to then get internships at their member companies because we know there are not enough trained, talented employees out there to sustain future growth. We’ve got to start doing that from the get-go. So again, didn’t want to echo the very remarkable comments that others have made. Wanted to kind of expand on some of the things that small biotech companies are concerned about.

I guess the one thing -- I will add one more thing, is that another heavy toll that COVID has taken on small biotechs is on clinical trial enrollment. So because of lockdowns, because of travel restrictions, because of the concerns for health that I think were absolutely legitimate, many small companies have not been able to enroll their clinical trials.

This, you’re going to see the effectiveness on a go-forward basis because these small companies will not have been able to meet their milestones, which may mean that their venture investors and their public investors lose confidence in the ability of these companies to execute. And you may see some innovation lost due to that. I think many people are trying to be very creative to address this issue, but it is another big burden that the COVID pandemic has put on life science companies.

MS. GARRETT: Thank you, Sue. Those were some very interesting observations. And I want to thank everybody for your observations. And I don’t know about the rest of the committee, but I actually found this very helpful and informative to see what is on, you know, different members’ minds from different perspectives. And I just hope that actually we can do this more often because I think this was really useful.

INCREASING CAPITAL ACCESS FOR UNDERREPRESENTED FOUNDERS AND INVESTORS

MS. GARRETT: So I think a lot of the things that were mentioned and have been mentioned by the Chair, the commissioners, and the committee members are going to be a nice segue into our second agenda item today, which is increasing capital access for underrepresented founders and investors.

Last August, this committee adopted findings encouraging the Commission to improve access to capital for underrepresented founders and investors. Specifically, what we stated, in addition to other things, was that we supported regulatory revisions to the capital-raising rules of ecosystem that promote increased opportunities for diverse entrepreneurs and investors.

And we asked the SEC to take leadership in that area. Today, I think we're going to dig a little bit deeper, see if we can come up with some more specific recommendations. The committee and our invited speakers over -- for different committee meetings have called for solutions that support smaller regional or emerging fund managers. We have heard that economies of scale generally result in larger funds investing in larger later-stage companies where smaller funds often target smaller and underrepresented founders, including founders in regions away from the coast.

Today we will dig in and discuss whether there are specific changes to the securities laws that could help improve equitable access to the capital via smaller funds. But first, the SEC Small Business Advocacy Team, which we find incredibly helpful, spent a lot of time looking at the data and the trends on small business capital formation, including the interplay of founder and investor demographics.

So to frame our discussion today, the team has prepared a brief data presentation on access to capital. Julie, Jenny, Martha, and team --

MS. DAVIS: I will take it away. This is Julie here -- my --

MS. GARRETT: Thank you, Julie.

MS. DAVIS: -- team -- sure. Can everyone see that? Can people see my screen?

MR. GRAHAM: Not yet.

MS. GARRETT: Not yet. No.

MS. DAVIS: Oh, hmm. Well, sorry.

MS. GARRETT: Yes. It’s starting.

MS. DAVIS: Okay. Got my pretty flowers?

A PARTICIPANT: Yeah.

MS. DAVIS: Awesome. Okay. Well, let’s see if now we can get some PowerPoint here. Struggling because I keep seeing you all, which is good, but I want to see my PowerPoint. Sorry.

MS. LEGG MILLER: Julie, would you like for me to share it from my computer?

MS. DAVIS: Yeah.

MS. LEGG MILLER: You run --

MS. DAVIS: If you don’t mind.

MS. LEGG MILLER: -- with the slide.

MS. DAVIS: I don’t know why I’m struggling --

MS. LEGG MILLER: I don’t.

MS. DAVIS: -- here. I will stop sharing, see if that --

MS. LEGG MILLER: Let me get that going.

MS. DAVIS: All right.

MS. LEGG MILLER: Got -- all right?

MS. DAVIS: Well, that works, so thank you, Martha, for the bailout. So, as Carla mentioned, we just wanted to frame the discussion with a quick refresher on some of the data that you -- we've shown this committee some of this before from our annual report. And so you may recall it. I'll go through it pretty quickly so that we can move on but did want to just -- there's some great data about small and underrepresented businesses in here. So if you want to go to the -- not the next slide but the one after, slide 3, Martha. Perfect.

As you can see here, there is broad diversity among new entrepreneurs. But unfortunately, as you'll see in later slides, the amount of capital raised is not similarly distributed, and minority entrepreneurs get a smaller percentage when it comes to getting funded. And this slide, I think, is really interesting because it shows the regional differences. It's the percentage of employer firms and what "employer firms" means is just companies that have a payroll so employer firms in each state that are owned by minorities. Next slide.

So as we heard this morning and have heard in many meetings prior to this morning, bank capital doesn't work for every business. And when you break down the data by race and ethnicity, it’s clear that minority businesses face even greater challenges in accessing it. Next slide.

So minority founders are also not as likely to receive VC funding as their White counterparts are, particularly challenging for African-American, Hispanic, and Middle Eastern founders who we see here received just 1, 2, and 3 percent, respectively, of VC funding. So this does -- despite the fact that ethnically diverse leadership teams have higher realized returns than companies with all-White leadership teams. So again, that’s data we explore in our report.

A PARTICIPANT: Come here, buddy.

MS. DAVIS: This slide is a -- shows a bright spot, which is that when diverse teams do raise capital, we see that they tend to raise more than all-White teams across successive rounds of funding. Focusing now on women-owned businesses, this slide gives an interesting breakdown of women business ownership by demographic group. Next slide.

Women founders raised less venture capital by headcount. They receive only 12 percent of VC dollars in 2019, and only 3 percent of the dollars went to women only -- next slide.

So -- and unlike the trend we talked about earlier where ethnically and racially diverse teams tend to raise more per round, women-led teams tend to raise less per round than all-male funding teams -- male founding teams. Also, the median VC pre-money valuation is lower for both all-women teams and mixed gender teams in here. So even just looking at the data on this slide, you can think through that when women are raising both -- both less capital per round and at lower valuations, together that means that women founders are giving up more equity than their male counterparts.

So -- and, you know, often the male counterparts are able to retain control of their companies through multiple rounds of funding. So women founders sometimes find themselves at a power imbalance that differs from male founders.

So moving on to -- from founders to funders, next slide talks about pattern matching. And this is a challenge this committee has certainly talked about, and we've heard speakers talk about. It's when investors -- the fact that investors tend to back founders who look like founders they've seen be successful before and who are familiar -- seem familiar to them.

The pattern matching perpetuates the cycle that concentrates capital in limited geographies, ethnicities, genders, and educational background. The next few slides will show that women and minorities are underrepresented among investors, which means, because of pattern matching, that tells us that founders are more likely to be funded by an investor of their same demographic background.

On this slide -- well, back to the -- the angel -- the angel at slide -- just quickly show that women and minorities lag in representation among angel investors, Catherine notwithstanding. Just 29 percent were women, and 7 percent minority -- 2019. And then moving on to the VC slide, so among decision-makers at VC funds, only 12 are women.

Three percent are Black, and 3 percent are Latino/Hispanic. So with women and minorities underrepresented at the funders who are deploying capital to these early-stage companies, pattern matching perpetuates the cycle. Next slide.

Another issue that first-time funds continue is -- another issue we’re seeing is that first-time funds continue to decline in size and number as well. And Sapna touched on this with her comments earlier. Emerging fund managers and smaller fund managers are important sources of capital for earlier stage companies, companies with minority and women ownership and companies outside of the coast where most of the mega private funds are based.

So moving on to show more recent trends and progress in diversity, the first -- next two slides show 2020 data comparing racial and ethnic diversity in VC firms. So in lighter blue, you see 2018 numbers, and in the darker blue, 2020 numbers. And the next slide -- this first slide shows all positions and junior-level positions. And then the next slide is -- this slide is investment professionals and partners.

The upshot is that for Black and Hispanic/Latino employee representation, there is -- you see a slight improvement in a couple of the categories, but nonetheless, the percentages remain significantly below percentages of the U.S. population at large for those groups.

But we can end on a more positive note with the final slide. And that is that although women still appear to be underrepresented in VC workforce, VC firms have shown steady progress since 2016 in increasing gender diversity among the junior level professionals, the investment professionals, the investment partners.

And it’s -- remember there’s junior-level positions that often provide a pipeline when filling more senior-level positions. So thank you, Martha, for sharing your screen. That’s it on the slides. I’m happy to take any questions or also happy to go about it as we proceed through discussions today.

MS. GARRETT: Anybody have any questions for Julie?

Okay. Thank you, Julie, for presenting that data. It was very useful, and I think it'll help frame our discussion today. The next segment is, in addition, our committee has heard from a number of speakers in recent meetings who have helped illustrate some of the issues that underrepresented founders face.

As many of you have acknowledged, we have heard more from these speakers than we could encapsulate in recommendations to the SEC at that time. So rather than inviting more speakers today, we have a highlight video of key insights shared with the committee by speakers from prior committee meetings, including on diversity, equity, and inclusion and capital raising. Jenny, are you going to show that video?

MS. CHOI: Yes.

MS. GARRETT: Thank you.

(A video was played.)

MS. GARRETT: Thank you. Thank you, Jenny, for that video. And I think that that video was a great compilation of what this committee has heard from speakers from various meetings. And we really appreciate the staff of the OASB for their work in putting that together. And next, Jeff and I continue to ask the staff to help us with different things. And for -- as a refresher for those of us who don't work with the specifics of fund regulations on a daily basis, Jeff and I ask that the team put together some cheat sheet slides on fund regulations.

And so Martha and Julie, would you like to present those slides to us?

MS. LEGG MILLER: Happy to do so. And again, with any cheat sheets comes lovely caveats that I don't even know that I necessarily have to make, which is that this is a gross oversimplification. But hopefully that means it is actually useful. So just to clarify, can everybody see my slide? Are we good? Yes?

A PARTICIPANT: Yes.

MS. LEGG MILLER: All right. Since no one said no, that we are good to go. So a lot of this came from resources that if you are listening as a member of the public, encourage you to check out -- they're on our website. One of the things that we've heard is there is a lot of jargon and legalese tossed around. And it's important to make the terminology in a lingo of capital raising more accessible.

So big kudos to our team and, in particular, Jessica McKinney, Jenny Choi, and Amy Reischauer as well as other members of SEC staff who put together a wonderful glossary. It is available online, and it will be linked in these slides when they are posted as a part of the meeting materials.

What I want to do is take some of the key terms, as Carla mentioned, and make sure that we are all starting from the same point just because there’s a lot of overlapping concepts. So three big overlapping concepts that we wanted to make sure we differentiate are the categories of regulation. So you’ve got regulation of the fund itself, generally under the Investment Company Act.

You’ve got regulation of the manager, a/k/a, the people. That’s the Investment Advisers Act. And then you have regulation of the capital raising process. That’s the Securities Act. And just wanted to make sure that we clarify those three different buckets because they each interplay with one another. Each have different registration and exemption regimes. And so want to talk through from a high level.

Two of those -- I think most of the committee members are pretty savvy with respect to the capital-raising piece. So starting with regulation of the fund -- and this is going to be fast. This is not a primer on all elements of securities law. But from a 10,000-foot overview level looking at types of funds which are often referred to among securities professionals as pooled investment vehicles, under the 40 Act, you had your registered investment companies on the one hand. And there's a couple of different types. And we have heard feedback in other meetings with respect to their role with small business capital formation. There is also exempt or private funds that you see. And typically that encompasses hedge fund and private equity funds, which are outside of the scope of what the committee, I understand, intends to talk about today.

And then we have venture capital funds. And that is a definition that requires a little bit more examination. So looking and zooming in on VC funds, we have heard -- and I think some of the members earlier today highlighted when they're talking about the 99 investor rule, that is coming from here as well as the 250.

Generally, under the Investment Company Act, you can break it down with two different specific exemptions. You've got 3(c)(1), which you see on the left, and 3(c)(7). Those are references to statutory provisions. The general rule that's been around for a while under 3(c)(1) is that less than 100 beneficial owners, all of whom are accredited investors, construct, which is how a significant number of funds are created.

In 2018, we got another type of 3(c)(1) fund, which is the qualifying venture capital fund. You heard in John McElway's (phonetic) comments during the video reference to that $10 million cap. That is on -- functionally the size of the fund needs to be under $10 million. But it allows you to have more than 99 investors. You can have up to 250.

Again, that's looking at beneficial owners. So it will look through different structures. So that number is actually a little bit lower in practice. 3(c)(7) funds, you heard that referenced in Monique's comments in the video with respect to qualified purchasers. There is not a limitation there on the number of investors, but they all must be qualified purchasers, which is a higher threshold than accredited investors.

And that looks to those with significant assets that are invested. So that's the high level on fund exemptions. And now I want to give the very high level on regulation of the manager so 10,000-foot view. Under the Investment Advisers Act, we have two broad categories that you can think about. One are registered investment advisors.

And depending on the size of the assets that they are managing, they are either regulated by the state or regulated by the SEC and a federal regime. Separate from the registered investment advisors, there are some managers who qualify under the exempt reporting advisor regime. Two particular categories that are worth highlighting here. One is the private fund advisors, which you see the criteria. They are solely an advisor to private funds with an AUM under two -- under $150 million.

And then the other is the venture capital advisor definition. And that is solely advisors to VC funds. And as you might guess, there is a specific definition carved out of what the VC fund means there. So for purposes of being an exempt venture capital fund advisor, there is really four broad criteria. And again, there is more nuance, as with all of this, to any of them. But the one that you -- I’m going to highlight here is No. 3, which is what we heard some folks referring to with respect to what some people call as that 20 percent nonqualifying basket. Generally speaking, 80 percent of the investments of the venture capital fund must be in qualifying investments.

So that does -- that generally means

investments in operating companies. So that would not count a fund-of-funds investment, an investment in a debt product as opposed to an equity product as well as some other different types of investments that a fund could make. So those would all need to -- to the extent that they're making investments as a fund in things that are not qualifying, it has to be less than 20 percent of the fund's commitments.

That is the very, very high level. I will not take any more time on that but again encourage anybody who is listening to take a look at the glossary and then reach out to our team if you have ideas and suggestions for how we can help distill some of these concepts and make the lingo about access to capital a little bit easier to navigate and decrease barriers to entry. So I will stop sharing my screen now and turn it back over to you, Carla, and the committee members for discussion.

MS. GARRETT: Thank you, Martha. Those slides were very, very helpful and should help guide our discussion today. I also have just looked at the jargon, cutting through the jargon on the website, and thought that that was a great resource and tool. And I think, you know, the public will look forward to looking at that.

Just in terms of a reminder on our timing, we will have a committee discussion until 12:15, and then we will break for lunch. And we will reconvene at 1:30, continue our discussion, hopefully make some recommendations, and we plan to adjourn at 2:30. So at this point in time, I was going to open up the discussion so that we can discuss potential changes to the securities laws or other solutions to recommend to the SEC to improve equitable access to capital through sophisticated investors investing in underrepresented founders via smaller or regional funds.

And due to our virtual setting, please indicate in the chat function that you would like to speak, and wait until you are called upon to speak. And following our discussion, we will deliberate on potential recommendations to the SEC. So is there anybody that would like to start? I might -- oh, Sapna, great. Thank you.

MS. MEHTA: If you've been in, you know, previous meetings, you know that this is a topic near and dear to me, as we would love to figure out ways that we can expand that cap or redefine it. Obviously, no one wants anyone to, you know, take advantage of the rule through tiering. I know the SEC has had concerns about that. But I think we can get around those concerns.

But I strongly believe that, you know, in order to get funding to the rest of America, you've got to open up those investment channels and allow larger funds to invest who don't want to become an RIA for a variety of reasons which I've spoken of in previous meetings due to the cost complaints, all of that. But if they want to remain an exempt reporting advisor, then, you know, to enable them to invest in these fund managers because we've discussed the challenges, especially for a lot of first-time fund managers, minority fund managers, you know, funds that are not on the coast. And it would really help to spread capital around and then allow those funds to invest in companies in their own backyard and, you know, really help that cycle. So I appreciate that this topic is being raised.

MS. GARRETT: Just to make sure that we're all clear on exactly what, Sapna, you were talking about, I mean, you're talking about the exempt venture capital fund advisor criteria and the fact that your funds can't hold more than 20 percent in non-qualifying investments. And fund-of-fund investments would be a nonqualifying investment and --

MS. MEHTA: Yes. That's --

MS. GARRETT: Yes.

MS. MEHTA: -- correct. So that under the 20 percent, you would have things I -- secondary purchases. You know, if you're buying shares from the founder, if it's not a primary transaction, that would be deemed to be a nonqualifying investment. And you would also have any fund investments that are not in operating companies count towards that 20 percent basket as well, the cap really so --

MS. GARRETT: And so just so we can have a discussion about it, are you talking about proposing that we exclude -- the SEC exclude fund-of-fund investments from that 20 percent nonqualifying investment basket? Is that -- or are you proposing that that 20 percent investment basket be increased, just so we have your specific thoughts?

MS. MEHTA: I'm not going to make a proposal right now because I would like to hear the concerns behind, you know, if we were to allow -- if we were to get -- carve out the fund-of-fund investments from that non-qualifying basket so they don't count at all towards that, you know, I know initially the concerns were that if you're going to be exempt, people -- you know, the SEC wanted that capital going directly to companies.

And I'm just curious to see if that thinking has maintained the same or if it has evolved. And so from my point of view, I don't see the reason for it.

But I would like to open up, at least have a discussion about what the concerns may be if it were not capped.

MS. GARRETT: Do people want to weigh in on that specific question of what the concerns would be if fund-of-fund investments were not part of the 20 percent nonqualifying investment basket? Do people on the committee have thoughts on that?

MR. LEE: Yeah, I can -- this is related to my question as well, which is -- I mean, obviously, I mean, Sapna’s question, that -- that line of issues, I think, is very, very important because you can apply the same kind of logic or questions Sapna had to other context as well.

Like for example, in -- even in the most recent SEC rules, there is now, you know, theoretically SPV available to be used for purposes of regulation crowdfunding. But I think a lot of -- people tell you it’s not going to work. So there is a lot of different rules, it seems like, that we have on the SEC perspective of fund management or SPV management, however you define it. And there is, like, all these, you know, individual rules or situations.

Some apply. Some doesn’t. And if there is some clarity of -- and my preference -- as you want it, there is a simple rule; right? If you’re managing a fund, this is what it is and then -- and then kind of everything else follows around it versus, like, this is the rule for this thing, and this is the rule for that when, at the end of the day, it’s basically -- like it’s an entity that manages money for a lot of different people. That would be helpful. And that was kind of -- so I personally think what Sapna raised is a worthwhile topic to delve into. And that’s related to my direct question, which is, this morning, obviously there was about probably at least 10 different distinct issues that were raised. Last sessions was pretty easy, at least in my mind, because I think the SEC had a very clear directive on -- or not directive but desire to change, for example, the private exemption rules, Reg CF and otherwise.

And there was a -- it was a pretty clear mandate. I think it gave us a little focus to kind of delve into the individual matters, especially related to, you know, company capital formation rules. I wondered if there was -- like if there is an official kind of agenda or desire to focus on, for example, investor or access to investors or -- sorry -- access to give or investors’ ability to invest in different opportunities because that would definitely help me, you know, focus on the topics that I feel might have more chance of actions versus just, you know, all the other things I could be talking about.

MR. SOLOMON: Carla, maybe I can -- maybe I can jump in and maybe try to -- I want to ask a couple of questions if I -- you know, just to get a general sense from the committee. There was one speaker who had mentioned sort of increasing the 10 million to 100 million. Let's just start with something as basic as that. And I think it would be great to hear from the committee if the committee actually thinks that's something that the -- very simplistic. Do we think that bigger funds or the ability to track bigger funds without any constraint is something that will -- you know, prima facie sort of change the dynamic because you'll get more coastal or professional investors interested in the possibility. How they choose to do that, we can deal with that.

But I just -- I want to understand at a very basic level if we think that going -- recommending from 10 to 100 is something that the committee thinks will change the dynamic or not. Like if people think that's not enough, people think maybe we need to have -- maybe it's too big. Maybe it's not big enough. I just kind of want to hear that first maybe as a jump-off point.

MS. GARRETT: Catherine, did you have thoughts on that?

MS. MOTT: Yeah. So mine’s more of a testimonial. We talked to some coastal VCs pretty much on a quarterly basis. And so maybe this will help provide an example of support for what Sapna is talking about. We hear from them is like, boy, this is interesting. These companies are interesting.

You know, if you could provide that 3- to 10 million to get them to a point, would we be interested in investing in them, in this specific company. Then we’ll come in, and we’ll be able to invest our 20 million.

On the other hand, you know, if they had -- so now I’m just saying that if they could act -- you know, take a portion of their funds and say, look, we support what you’re doing. We’ll invest in your fund locally because what we like about that -- and that is true. This is what they typically say -- right? -- is early-stage companies are hands-on and need lots of support, and we’re not going to fly from California or Boston on a regular basis to oversee, you know, what’s happening and give them the support they need.

We need to have, you know, hands-on. They need to have hands-on support. So having said that, I think -- I mean, what I -- what I value great -- greatly about the Rise of the Rest Revolution Venture Fund, whatever, is, you know, they've gone where no one else has gone. And giving them the capacity to, you know, support smaller funds in the regions, across the Midwest, could be hugely beneficial.

So in a way, you know, if a large fund on the coast could say, okay, I can go -- so Jeff, if I understand -- so I don't understand the regulatory piece so well. So if I could do more than a hundred million of my fund because I have, you know, 1.2 billion under management; right?

So why not be able to support some of the Midwest funds and distribute that accordingly as a -- you know, maybe larger than 20 percent of my fund would be a fund-of-funds, you know, investing and other funds where they're close to the company. They're giving them the support. They're getting them to the point where they can, you know, now justify a 20 million to $120 million investment. I mean, am I -- am I on the right track? I'm not sure. You're muted, Jeff.

MR. SOLOMON: Sorry. First-time Webex user. Just kidding. You know, I think it's two different things but they're -- they're interconnected.

MS. GARRETT: Okay.

MR. SOLOMON: You know, there is -- as Sapna mentioned, there is definitely a reluctance on the part of a lot of VCs to become registered investment advisors. And there are exemptions to becoming registered, either the fund being registered or the advisor being registered. And that's kind of what -- what Martha was doing when she was walking through these various areas.

So before we try to navigate that, you know, there's an idea here that you -- you know, if you could use one of the exemptions, the $10 million makes it completely irrelevant. So if you were to be able to raise $100 million. Let's say it's $100 million sidecar vehicle. By the way, anybody could raise. It could be a Midwestern VC, or it could be a coastal VC. People with access to capital, they might wake up and try to raise a hundred million dollars.

If it's a hundred million, it might be, almost by definition, a coastal VC who has the access to that kind of capital. But they're only going to do it if they think that they're not going to be registered. So it gives them an opportunity to think about how that hundred-million-dollar vehicle dovetails with their -- with their main vehicle.

So the way that most VCs I know think about it is they're interested in sourcing future deal flow. So if you can get highly qualified deal flow and then that's fantastic for your big fund; right? You just don't want to burn a lot of energy looking at a lot of small companies because you know the vast majority of them aren't going to get to a level where you can invest meaningful capital. But the structure of venture is they'll -- if they can take a hundred million dollars either and invest it either in local funds or in sidecar vehicles with local funds for the best ideas coming from that region, they will do that because it gives them a future pipeline of investments to make at the 20- or $50 million level for their bigger funds.

So this is about creating an on-ramp, a capital formation on-ramp. And so I think what you've highlighted is, you know, the ability to take capital into your fund as a qualified, you know, fund in -- a qualified seed or venture -- early-stage venture fund in your region. You should be able to take capital in. And that's what Sapna was talking about, like limit -- the limits to funds making investment in other funds. We should consider that.

I think I'm also saying if we get to using the hundred-million-dollar -- using the exemption that goes from 10 to a hundred or making that recommendation will actually help coastal VCs to think about raising specific funds that they can use to build their pipeline of future investments. And maybe we angle that towards non-coastal investments, or we try to get them to target that with some rules. But it’s a combination of both this idea of raising the exemption, as Sapna mentioned, as well as raising the aggregate amount so that we can get them to actually think about how to build their own pipelines, which they would naturally do; right? Does that make sense? Carla?

MS. WASHER: Yes, it does. So I just had a comment that I wanted to add. I’m completely in agreement with what Sapna just -- and Catherine has said. And I just wanted to point out why this is logistically a problem.

So, you know, it’s almost a -- a feature of some of the VC firms’ success. If you think about an MPM or an NEA or one of the big firms, they’ve raised hundreds and hundreds of millions of dollars, but they have X number of partners. Those partners can only sit on so many boards. So you take the amount of money they have, divide it by the number of partners they have and divide it by the number of boards they have.

That’s the size check they have to write because otherwise, they can’t keep track of their investments. And so that’s why it’s important that we are missing this middle size fund where there are four or five partners and 150 million -- 100-/150- -- I don't -- doesn't matter. So then you divide the 150- by the number of partners and the number of boards, and you can write a 5- or $7 million check, which is what, you know, you needed.

And I agree completely, Jeff, that the bigger funds would completely support that because, you know, fund for them that they can put 20, 30, 40, 50 million companies for them that they can put that much money and don't spring -- made from the earth. They're invested in at a much smaller stage.

And so we need to figure out a way to have the regulations support the viable creation of these mid-size funds to feed into the larger funds.

MS. GARRETT: Thank you, Sue.

Jeff, would you like to go ahead and continue navigating this? Greg?

A PARTICIPANT: Go ahead, Jeff.

MR. YADLEY: Can I just add a quick comment? I agree with these prior comments and also something that hasn't been mentioned. Diversification is really important, particularly in an area like this where most investments are not going to be home runs or even work out particularly well.

So $10 million is pretty low. This would allow diversification --

MR. SOLOMON: Did we lose him?

MR. YADLEY: Too low of a limit and 506 is unlimited. It doesn't mean that people are going to raise $100 million funds, but it definitely gives them more flexibility. I'd also like to follow up Sapna's question and try and get educated a little more about the 20 percent limit, which I've always -- for nonqualifying investments in venture capital area.

I've always understood that to be that you're not supposed to be creating an investment fund where you're investing in securities.

You're supposed to be investing in operating companies. So as long as the fund-of-funds that you invest in are investing in operating companies, that shouldn't be an inhibition to allowing that.

So I would support that but agree that we should make sure there's not some other mischief that has been done in the past that we're trying to guard against there.

MR. SOLOMON: Right. But Sapna, I just want to understand a little bit more because I think that what's not clear is whether or not an investment in another fund is a non-qualified investment. Or maybe it is clear, and we're trying to figure that out. So, you know, I'm not sure that it's opening up the aperture a hundred percent to, you know, basically allowing whatever -- you know, anything goes. But I think it -- it would be helpful to hear from Sapna if there's a specific exemption that she's looking for on the fund-of-funds side that would open it up.

MS. MEHTA: Sorry. Your question is -- I thought it was -- so if we wanted to invest in another fund, are you asking if that fund makes other fund investments? Would we -- are we asking for an exemption for that as well or --

MR. SOLOMON: No. Let's take a real-world example. Like let's talk about specifically what you're doing at Rise of the Rest, which might be a model for others; right? Rise of the Rest is attached to a bigger fund; right? You use Rise of the Rest as a way to source other opportunities and specifically targeted towards smaller investments in areas not on the coast particularly.

I mean, you might do stuff on the coast, but you've got a specific mandate to try to look beyond that -- right? Just for clarification.

So if Rise of the Rest decided that it wanted to put a significant portion of -- or some portion of its investment in local VCs -- right? -- are you saying that that right now the way that -- is a question I have. Are you saying that, right now, that would actually fall into the nonqualified investment bucket?

MS. MEHTA: Yes. So any investment in another fund falls into that 20 percent bucket. And --

MR. SOLOMON: Right. So what I'm -- sorry. I'm sorry. I didn't mean to cut you off.

MS. MEHTA: No, no, not at all. And I'm just saying that even though there is that flexibility to invest up to 20 percent, practically speaking, it makes it a little more difficult because then you're choosing, you know, which fund managers you're going to invest in.

And when you're a fund like us and we are trying to -- we have a network of relationships across the country. It's just -- it's harder to pick and choose amongst, you know, so many very --

MR. SOLOMON: Funds.

MS. MEHTA: -- friends and you know --

MR. SOLOMON: Right. But that's not the only aspect of a nonqualifying investment. There are many other --

MS. MEHTA: Correct.

MR. SOLOMON: -- elements in that. So if you decided to do follow-on offerings in a private investment in a public equity because you wanted to step up at an IPO and buy public shares for a company that was going public, that also is included in your 20 percent. And what I'm saying is maybe, Greg, the right way to think about, without being too prescriptive -- the right way to think about this is we should just exclude investments and other venture funds from nonqualified.

In other words, a fund that is $100 million fund that is otherwise exempt can invest up to a hundred percent of its funds in other funds if it wants to do that without triggering the 20 percent. So we don't have to open up the whole definition of nonqualified investments.

We can simply say that fund investments in other funds that qualify are no longer part of the 20 percent. They can just be general. That's what I was suggesting. Does that make sense?

MR. YADLEY: It makes sense to me subject to -- the original question was why is it there. And if it's there simply to assure that we're not creating a mutual fund -- we're actually creating investments, you know, passive investments in these companies and some with little more than just passive then -- then that sounds fine to me. But I -- some issue that was being addressed or it’s just historic and -- because there didn’t used to be funds of funds as prevalent as they are now.

So maybe we could ask the enforcement division, you know, have -- have Martha’s office just to see if there’s information where there would be an agency objection to this because it does seem to be a limitation without much of a purpose today.

MR. SOLOMON: Okay. So the second thing we talked about is -- again, I just want to know if anybody’s got a visceral reaction to making a recommendation.

Again, I don’t want to be too prescriptive because we’ll talk about this in the subsequent discussion, or maybe we should just think about this now as we head into lunch, Carla, and then come back and maybe do -- be a little bit more prescriptive about the idea of increasing the size of the fund so that we can start to attract people who have access to that kind of capital as well.

Again, anyone can weigh in, but maybe that’s just something we should canoodle on over lunch because I know we’re going to get up on time here in a few minutes. If anybody wants to comment now, please feel free, but we can pick it up after lunch if you want to.

MS. WASHER: If what you're talking about is raising that cap from 10 million, I think that that absolutely needs to happen. I would be very supportive of that recommendation.

MS. MOTT: I believe it's in -- you know, me too. I would be very supportive. And it almost feels like a no-brainer to me. We have people who are making angel investments, but they could -- you know, but we limit the fact that they can participate in a fund that's going to, you know, invest maybe further upstream.

To me, you're -- you know, you're -- you're spreading your risk a little bit better and expanding, you know, the way you address that asset class with a little bit less risk. So I'd be super supportive of that. It's definitely needed in the market, particularly here in the Midwest.

MS. GARRETT: And Jeff, the other thing that I think we heard a lot of this morning was the 99 rule so limit on accredited investors. And so maybe that's also something that, you know, people can think about, and, you know, we -- you know, after our lunch when we come back, we can discuss that as -- you know, as well as other areas, too, that people have.

Are there other areas that people want to kind of just bring up right now so that we can be thinking about a little bit over lunch so that we have kind of a bit of a structure for just remaining time after our lunch break?

MR. SOLOMON: I just have one question. And I know I always end up talking about where the investors come from, and that's not necessarily the purview of this committee. So it's really more for the staff. Are we willing to entertain, you know, exemptions for things like accredited investors for underrepresented investor groups, or is that something that we should just leave to the purview of the Investor Advisory Committee?

MS. MOTT: I think we should address it, Jeff. You know, it started here with our committee. We should continue to support it. So -- and I think others have spoken up. I know a lot of people left the meeting here, but I believe Youngro was very supportive of this as well. So I think this committee that -- I mean, this is -- Greg, I think we asked for this about three terms ago. I don't know. But, I mean, it's something we've been certainly supportive of for a long time, and I think we should remain supportive.

MR. YADLEY: I agree.

MS. WASHER: Agreed.

MR. SOLOMON: Yeah. I mean, my question was more is this something that we should be trying to craft, or do we just want to be supportive of other advisory groups that may be exploring this in more detail? I mean, I think for sure we'll be supportive. I know this -- I mean, this group has been very outspoken on it. I think we have as pretty close to unanimity on our support for getting inclusive -- creating opportunities for investors who might not otherwise qualify for these investments to get included in the capital formation process because there's wealth creation that occurs there. So I think we should reiterate our support for that. I guess it was more --

A PARTICIPANT: Right.

MR. SOLOMON: -- of a question for the staff. Is that something that you're -- we would be looking for a recommendation on, or is it something we should simply reiterate our support for and then allow the Investor Advisory Committee or other folks who are really working on the capital sourcing, like where does the capital come from, to try and address that specifically.

MS. LEGG MILLER: Jeff, I think that that's a great question and one that is up to the discretion of the committee. It's one of the areas that overlap with other committees, so it's not one that -- you know, it falls within the enabling legislation of the purposes for which this committee was created, and the extent to which the committee would like to address that is certainly something that each of us would -- all of you on.

MR. YADLEY: Yeah. Jeff, I think all of us, as -- when we take the responsibility of being on an advisory committee, we -- and advise the Commission, we have to recognize the Commission has three prongs to its mission. And we happen to be focused on capital formation, but we're also very mindful of investor protection. That's a different viewpoint than the investor committee, which is focused more on investors and, based on some of the recommendations, the protection of investors, so I think a healthy dialogue among all interested parties, which includes us. We should definitely weigh in.

MR. SOLOMON: Okay. Carla?

MS. GARRETT: Yup. Sounds good. Thank you guys for that. And so it's 12:15. We will now break for lunch. The webcast will be stopped during lunch, and it will resume at 1:30, so if the members can jump back on about 1:25, we will see you then, and we will look forward to our afternoon session. Thank you.

(Whereupon, a luncheon recess was taken at 12:17 p.m.)

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

MS. GARRETT: Welcome back, everybody. I hereby call the meeting back to order. We are joined now by Commissioner Lee, who, with arrival of Chair Gensler last week, wrapped up her service as acting chair. Commissioner Lee, thank you for your continued service, and thank you for taking the time to be with the committee today. We look forward to hearing from you.

COMMISSIONER LEE: Thanks, Carla. I'm sorry that I couldn't join you this morning and thanks so -- thanks for letting me kind of horn in on your afternoon instead. I don't want to cut into your session too much, so I'll be brief. Let me start, as always, by thanking this committee for its work. And I especially want to thank you all for revisiting the topic of increasing access to capital for underrepresented founders and creating opportunities for diverse investors.

Your recommendation to the Commission last August urging us to promote opportunity for diverse founders and investors was a good step forward. And I appreciate that you're spending additional time today to help us think through specifically how to tailor policy changes that can achieve that goal.

There's a lot of data showing us there's a problem, and there's a pretty good consensus that we need to do something about it. But it's quite a challenge to roll up your sleeves and do the work of coming up with concrete solutions. So you are all doing that important work, and I'm grateful, and I look forward to seeing your recommendations.

As we think through these issues, one thing I think the Commission needs to confront is how we go about assessing the effects of our rulemaking on underrepresented and marginalized communities. Are there likely to be disproportionate costs to certain segments of our population from our policymaking, and how can we be sure that the benefits of our rules will actually make their way into these communities?

If we do undertake specific policy initiatives, for instance, to increase access to capital for women and minority-owned businesses, how do we analyze whether those policy choices will have the intended effect? I've talked before about certain steps I think the Commission should take to better incorporate diversity considerations into its policymaking.

The first is incorporating our Office of Minority and Women Inclusion into our rulemaking process to help ensure that we're leveraging all the expertise we have at the agency on these topics. And the second is incorporating into our economic analysis an assessment of the cost and benefits of our rules on different segments of the population.

On this latter point, I think it’s time for the Commission to formally incorporate an assessment of the distributional consequences of our rulemaking into our economic analysis. This is likely to happen at other agencies. The Office of Information and Regulatory Affairs and the Office of Management and Budget have been tasked with formulating recommendations for modernizing the regulatory review process, including incorporating procedures that take into account the distributional consequences of regulations. That is procedures to ensure that regulatory initiatives appropriately benefit and do not inappropriately burden disadvantaged, vulnerable, or marginalized communities.

The idea that agencies should be incorporating distributional analysis into their rulemaking is not new, but it’s an idea I think whose time has come. And when we look only at the overall cost and benefits of our regulations, we do a disservice to communities that tend to be overlooked and marginalized, and we miss opportunities to better calibrate our rulemaking to achieve the desired effects.

So I hope our Division of Economic and Risk Analysis and Office of General Counsel will revisit the current guidance on economic analysis and consider updates including how to better capture difficult-to-quantify benefits of our rulemaking and, importantly, its distributional consequences. I think doing this will enable us to better implement any recommendations like those that are being contemplated by this committee today. So again, I thank you all for lending us your time and your expertise, and I will leave it at that. Thank you, Carla.

MS. GARRETT: Thank you, Commissioner Lee, and thank you for joining us.

INCREASING CAPITAL ACCESS FOR UNDERREPRESENTED FOUNDERS AND INVESTORS (CONTINUATION OF PREVIOUS DISCUSSION)

MS. GARRETT: Okay. Now we're going to turn back -- our session back to what we were talking about before lunch.

Jason, welcome back to the conversation. You missed a lot. So, well --

MR. SEATS: Sorry to miss.

MS. GARRETT: I'm joking. We are just glad to have you here and glad everybody else joined too. We talked about a handful of issues. I'll do a very brief recap. We talked about the -- with respect to the venture capital advisor exemption possibly excluding fund-of-fund investments from the 20 percent nonqualifying investment basket.

We also talked about with respect to the qualifying venture capital fund exemption, increasing the $10 million limit. And I wanted to open up the discussion to see if people wanted to talk in more detail about each of those and then also bring up other points that people would like to talk about.

Let's start with the $10 million limit and whether we think that increasing that limit in a qualifying venture capital fund exemption is a good idea. I think we've heard from many people earlier this morning that they did think that that was a good idea and just wanted to continue to get feedback on that.

MR. SEATS: Hey, having missed that session this morning, I'll just add that I think it's a great idea and will have a big impact. Are we debating or proposing a new limit?

MS. GARRETT: That's up to the committee. What do people think?

MR. SOLOMON: We were talking about 100 million but only because it's a round number. I don't think we really actually chased that down. Does anybody have a different point of view?

MS. MOTT: I would propose maybe even up to 150-. The reason for that, again, you know, when you look for institutional investors, you know, they will not -- you know, so primarily I would see this -- this rule would apply to being able to aggregate money from accredited investors.

So let’s talk -- so qualified investors, so particularly institutional investors, won’t invest unless you have at least a $200 million fund because they -- you know, they have to deploy 20 million. You know, they are managing such large amounts of money. It doesn’t make sense for them. You know, we totally understand that.

But it makes it almost impossible for emerging managers to raise a fund and address, as I mentioned earlier, a much-needed market space -- marketplace that the Series A round is really becoming known as the Valley of Death. And we’re talking about for good companies, not bad companies. I’m talking about -- I’m not talking about putting bad money after -- or good money after bad. I’m talking about putting good money into companies that have certainly proven that they can continue to scale and cross that -- you know, cross the chasm and continue to prove their worth in the marketplace.

So having said that, Jeff, I would propose 150 million. If we had to back down, I'd back down to 100. But it seems to me yesterday when I talked to a fund-of-funds, he said our minimum is -- he said it's lower than most, and ours is 15 million. So it has to be at least 150 million to attract institutions so maybe up to 150-. I would like us to consider that.

MR. LEE: I would actually support that, Catherine, and mainly because the $150 million is an actual number in the private fund exemption as well. I really loved how Martha in one of her presentation had the -- like literally different kinds of exemptions for funds as well. And, I mean, if we think about the logic of the private fund registration exemption framework, it's just as convoluted, in my opinion, as kind of we talked about last year, which is the general securities offering exemptions.

We want to have some consistency and -- if the private fund exemption, as a matter of principle, can manage up to $150 million as long as you're managing private funds -- registered, I actually don't see a difference necessarily on why that shouldn't apply to the venture capital exemption. And that's also because, in reality, I mean, I think the -- rules were, I think, as a result of Dodd-Frank, whatever, 15 years ago, a little less than that.

So the world has changed. I mean, literally the world has changed over the last 10 years. What typically venture capital exemptions or angel investors presumably back in 2007 were investing in I think has changed dramatically given where the world is. And so if nothing else, for administrative simplicity, I like that 150 million number because it, you know, adds onto what -- the framework we already have in place, an exemption that we already have in place for registration.

MS. MOTT: Jason, I have some context to your question about why the $10 million rule. It was arbitrary. We were very -- when I say “we,” Angel Capital Association was very involved with the legislation that was established with the 250 investors and going to 10 million. The cap was created, actually, as a -- I would say a negotiated effort between both sides on the aisle.

At the time, I think that the request was for make the cap 50 million. And then it -- for some reason, it was like this is all you’re going to get. Take it. And so everybody said yes. We’ll go along with it and sign off on the legislation. So that’s just -- now, that’s really rough. That was -- that’s rough from my memory.

MR. SEATS: Got it. That's not a great story.

MS. MOTT: No, it's not a great story. It's not a great story.

MS. GARRETT: Anybody else have any thoughts on that dollar amount or that specific increase?

MR. SOLOMON: Listen. I mean, I always -- in this particular case, a greater amount is probably better just -- people don't have to raise 150 million. They can raise up to 150 million. So if we give them the flexibility to do up to 150 million, some will raise 100-. Some will raise 150-. Some will raise 75-. I think once you get sort of much above that, now you're starting -- you know, I just think about a bunch of the traditional venture funds. And I'm a little bit concerned about having these exemptions be too big because we do see price distortion and valuation distortion.

And so the bigger -- I mean, that's something that's happening; right? The venture funds have become billion-dollar venture funds. They have to write bigger checks. The valuations had to be bigger. I think 150- feels right to me. I wouldn't advocate for much more than that because, you know, we're not really trying to create inadvertent price inflation on private security investments. And 150- feels like it slots in nicely underneath the size of a lot of venture funds today as a -- this idea that we can create feeder -- feeder vehicles.

MS. WASHER: I agree.

MR. LEE: I mean, it’s probably, Jeff, not just the 150 million that’s -- it’s actually the underlying investor. I think the venture capital exemption is 249 investors or whatever. The number of investors in the fund, in general, the 99 person, I think -- I don’t know. Someone mentioned that earlier. Like these are all related. It should -- because you can increase the cap. But if you don’t allow more investors to invest, you’re basically now ironically, you know, going after bigger-checked investors. So I think the amount of cap of the investment funds that they can raise without being subject to full RIA registration, it probably should be thought of in concert with, you know, can we open the funnel from the investor base as well to match that.

MS. MOTT: And I would -- keep in mind what we’re doing, is we’re serving a point where the baton gets passed. You know, the seed funding, you know, friends and family, then seed funding, then Series A and then Series B. At that point, Series B, the large VCs come in. It’s that Series A that -- you know, there is a huge gap in the marketplace. So we’re bridging a gap with this.

MR. SEATS: Yeah, I -- something I’d inject into this when we think about how to observe the impact of a change here, assuming that we have a change, is getting a little better understanding of the dynamics of the -- of a firm that size. And I think one of the main challenges with the 10 million number is that’s not actually big enough to be a viable venture fund. Like there is not enough money to cover paying yourself a salary if you’re a single GP by yourself, one person trying to do the thing. And so there -- you can back into reasonable sizes of some of these things by just looking at, like, the composition of a firm and how does it look and what level of assets per human employee of the firm makes sense. And I don’t know -- I’m not sure what the best numbers are there, but I’d say it’s probably, like, 25 to 30 million per investing partner for a traditional -- pretty traditional fund.

And so if the thing you’re looking at here is what does it take to help encourage capital formation for an underrepresented investor in an underrepresented area who is going to, by -- almost by definition without even trying implicitly direct capital towards underrepresented founders. And you want them to have a viable business doing that. You know, three people doing that, probably would want to raise somewhere between 50 and $100 million fund if they could pull it off.

And so I think trying to think about, like, what -- what the dynamics of the firm are might be a useful thing to sort of keep track of, too. And those market -- does change with market conditions also.

MS. GARRETT: Thank you, Jason. I think -- and Catherine. Those are both, I think, very good points around the reasoning why this would be a useful increase.

Youngro, with respect to the number, the qualifying venture capital fund exemption allows 200 -- up to -- yes.

MR. LEE: So I think -- so just to clarify that, what I meant was so the exemptions, when it was created under Dodd-Frank, I assume people were thinking about kind of the issues we’re talking about here. But nobody -- just like the JOBS Act, at least the very first version, nobody actually knew; right? Like they just came up with these rules. So I think what we’re saying now is that the industry has evolved.

The community has evolved. And, frankly, the number of people interested in investing in these funds, which I think people agree is generally, for the average investor, better than investing deal by deal because you do get the benefit of the portfolio allocations. So if that’s the case, having the 249 number at minimum should be consistently applied across the increase to -- whether it’s 100-, 150 million. But I would argue even more; right? Like just pick one.

If it’s $150 million, like, let people invest as long you’re creating investors until you meet the limit because otherwise, you’re still going to be going after the same type of investors to fill numbers. And then the 99-person rule is obviously for probably the fund exemptions. And that’s what, I think, the other gentleman from the previous -- the video -- someone was talking about it.

The 99 figure is also arbitrary. So I think that’s kind of where you can’t think one -- the other because the institutional investors that are allocating their money to these smaller fund managers, they themselves -- like everybody has a master. Everybody is subject to some rules that they have to allocate to. But if we’re really -- if the goal of this rule is to allow an average person -- and they can be accredited. You know, that’s a rule.

If the goal is to increase participation from more investors to access, you know, different type investment opportunities, more underrepresented -- you know, intended for underrepresented founders and minorities and communities, all that -- all that, we have to allow -- basically increase a number of limited investors for 3(c)(1) purposes, you know, to be on 99. So basically, like, my one recommendation really is not just think about the cap but just somehow increase the number of investors, whether 99 or 249, depending on the exemptions.

MS. WASHER: Well, when I look at these definitions of the 3(c)(1), there is the generally, and then there's the qualifying venture capital fund. And there -- and there's two different -- you know, I think we've spoke about earlier is that why are we creating all these very confusing rules? Why not just say a 3(c)(1) is 250 beneficial owners and 150 million?

I mean -- and not have the two categories there because it just -- it just seems like we're creating a lot of complexity that we all agree right now isn't working.

MR. LEE: I would a hundred percent agree with that, and I would love to have -- I mean, I love this committee and the commissioner when we're talking about regulation crowdfunding, Reg A, Reg D. The philosophy seemed to be how do we make these consistent. And I absolutely think there is an opportunity to do that in the private fund registration exemptions as well. And I think everybody does agree, like, it is, all things considered, you know, better to invest in a fund than one investment from a risk management perspective.

MR. SEATS: I totally love the idea of aligning the qualifying venture capital, the $10 million things just be the same as a 3(c)(1). I would worry about the sort of discontinuity of the 3(c)(1) to 3(c)(7), then, if the setup is, hey, can't raise anything bigger than 150- under the 3(c)(1), and then you flip over to 3(c)(7). That means accredited investors get removed from the ability to invest in 3(c)(7) funds unless I'm missing something. Maybe there's a way to do that with a feeder or something that's just -- I don't know. But like --

MR. LEE: I think, Jason, on that, I think -- I mean, so this is where this -- these gets really technical. So it's -- to be clear, we're not -- to make it worse, more confusing, the venture capital exemption, accredited investors can invest, but our typical private funds under 3(c)(1), assuming they're charging carry, it's not just accredited investors. It's qualified clients, which is you have to be worth at least $2.1 billion.

MR. SEATS: Yeah.

MR. LEE: And if you want to do beyond that, now it's qualified purchasers. You have to be worth $5 million. So again, like, this is very -- I just know it because I'm fund's lawyer.

MR. SEATS: Totally.

MR. LEE: Have no idea; right?

MR. SEATS: I thought the suggestion was to have -- to sort of get rid of this $10 million weird thing and just raise the investor count limit of accredited for 3(c)(1).

MS. WASHER: And then you would still have the 3(c)(7), which are qualified investors.

MR. SEATS: Right.

MR. LEE: What I'm saying is if you do that, we would have to also make sure that -- like we -- I think -- this is more for the SEC, but we'd have to be very specific with our rules because under current rules, unless you're on the venture capital exemption and the other rule, it's not just accredited investors. You have to be a qualified investor. So the threshold was actually higher. So I think we have to --

MR. SEATS: For a 3(c)(1)?

MR. SOLOMON: Yeah. Let’s be careful. I do think we need to be careful here because 3(c)(7) and 3(c)(7) are broad applicability beyond venture.

MR. LEE: Correct.

MR. SOLOMON: Okay?

MR. LEE: Right.

MR. SOLOMON: So -- and there’s just -- we do not want to get in a situation where we start opening everything up under 3(c)(1) and 3(c)(7). I would suggest, respectfully, that we leave them alone. There is a different path specific to venture where we can accomplish what we want to accomplish by just addressing the venture capital exemption which already exists. We’re just talking a matter of size and maybe investor count, which is fine. And I would just -- I would just stick with that because once you start messing with 3(c)(7) and 3(c)(1), you’re just going to have a lot of people weighing in on areas you just don’t want people weighing in on like are hedge funds going to be exempt and the hedge fund community is going to be out there asking for, you know, special exemptions.

I just -- you know, there is a -- there is a thing that goes on between the hedge fund community and the venture community where one has to be registered and one doesn’t. And that’s a tension point and so --

A PARTICIPANT: Yeah.

MR. SOLOMON: -- there is just no -- there is no reason to even bring it up. Let 3(c)(1) and 3(c)(7) do whatever they do, and let’s focus on the -- my -- respectfully, my advice would be to -- let’s focus on the venture capital exemption that already exists and just try to tweak it so that we can make it bigger and more usable.

MR. LEE: Jeff, I 100 --

MS. GARRETT: Can I ask --

MR. LEE: -- percent agree with that. Apologize. One follow-up comment is the only reason why I’ve been bringing the other concepts up and for the -- the rest of the committee to know, the venture capital exemption as defined today will not allow those funds to invest in the kind of small business we’re talking about and the kind of forms that we’re talking about. It's -- you have to have certain definition of the venture capital portfolio company. So it would not allow loans.

It will probably not allow investments in small businesses, like the true small businesses, so that’s just one comment there why -- if we’re going to do this -- and the underlying goals of the funds is to also invest in local small businesses. And it might not be. That might be a policy decision, but I did want to flag that the venture capital exemption does limit the type of investments those funds were able to be paid.

MS. GARRETT: Youngro, are you saying that under the 3(c)(1), qualifying venture fund capital fund exemption that there's limitations on the types of investments that those funds can invest in under --

MR. LEE: Someone, Jason or Sapna, might have a better idea but --

A PARTICANT: Yeah.

MR. LEE: -- understand it was -- there is a pretty specific definition of what constitutes a venture capital investment.

MR. SEATS: It's a qualifying venture investment, which has a definition. And it's a primary equity purchase and -- and it's not debt, so you do -- you do have to track how much debt investing you do. If it's -- even if it's convertibles, I think, against a 20 percent cap at the -- at a fund level for --

MS. GARRETT: Well, are we talking about two different things here, or are we -- and Martha, Julie, tell me if I'm right or wrong. But are these interrelated? Are these the same, or are these two different things?

MS. LEGG MILLER: Yes. So it -- they are related concepts. So if you pull back up the slides that we had, actually, just quickly so that you can see --

A PARTICIPANT: Here. I can -- I have it up. I have it up. I can probably figure out how to do it.

MS. LEGG MILLER: Got it. Come --

A PARTICIPANT: Okay.

MS. LEGG MILLER: -- here. All right. Can you see this?

A PARTICIPANT: Yes.

MS. LEGG MILLER: And apologies --

MS. GARRETT: Yes.

MS. LEGG MILLER: -- that it's not in presentation mode right now. But if you look, you see right here one of the criteria for the qualifying venture capital fund is not only the $10 million and the less than 250 beneficial owners, but it is also the VC fund piece, which you will recall are these criteria right here, which is where you pick up the qualifying and nonqualifying investment. So that is where you have -- instruments excluded, secondary shares, fund-of-fund investments, and digital assets, among other things. Does that clarify?

MS. GARRETT: Yes, it does. So going back to the slide, the first one that you showed, under the 3(c)(1) funds under "generally," the ones that are a hundred -- if you only have 99 beneficial owners that are accredited investors, that does not need to qualify as a VC fund because it doesn't --

MS. LEGG MILLER: Correct.

MS. GARRETT: -- have the asterisk there?

MS. LEGG MILLER: Correct.

MS. GARRETT: Okay.

MS. LEGG MILLER: Correct.

MS. GARRETT: Okay.

MR. LEE: That's correct, Carla. But then again, if you're charging carry so managers under general 3(c)(1) funds, if they're charging carry, they can only use that money from qualified clients, which is you have to have net worth of $2.1 million, whereas on the venture capital fund, you can just be a regular accredited investor and the fund manager can still charge performance fees, is my understanding.

MS. WASHER: Aren't we talking about, though, this qualifying venture capital fund and changing that $10 million number? That's what we're talking about -- right? -- is changing that $10 million number to be bigger in the 100-, 150- range so that it really fills that hole we're talking about. And then aren't we also talking about making the -- in general, making this 99 a bigger number? Isn't that what we've been discussing?

MS. GARRETT: We've definitely been discussing making the 10 million bigger. I think the proposal on the table is up to 150 million. What I've heard that we're also talking about is kind of two things. One, whether or not we try to combine. I think some -- Youngro's suggestion was combining the general and the qualifying venture capital fund exemptions into one to kind of harmonize it and streamline it and make it easier.

Other people have said maybe we want to increase the 99 beneficial owners. So those are, I would say, two different thoughts on the table with respect to the 99. Separately, 10 million up to 150 million seems to be what people are interested in. So maybe we could flesh out a little bit more whether we think that it is good to have the two prongs of 3(c)(1) under one.

And this is where I think Jason and Catherine and Youngro, the other people, Jeff, everybody in the industry other than me who is not a -- who is a securities lawyer can really talk about, you know, do you guys like having the two prongs, and do we really just need to increase the dollar limit, or do we think we also need to increase the number of investors?

MS. MOTT: I think it needs to be both. And let me say why I am thinking this. I'm thinking that when you're a larger fund under the hundred, you know, investor rule or 99 rule, you're raising money from a whole different source. You're raising capital from institutions. And they will -- I mean, they invest, you know, at 20 million plus in funds. And so that is why it's easy for large funds to -- you know, to exist. The smaller funds are aggregating capital from high-net-worth individuals, family offices. So what we get in the smaller funds is mostly accredited investors and maybe some that would come under the -- you know, they have 5 million under management. So it might be, you know, some of that type.

I think if we really want to have a meaningful impact in the space that needs it the most, that Series A round, I think we have to increase the number because most of that money will come from accredited investors. So we're looking at people who will invest, you know, anywhere from a hundred -- 125- to a million dollars. Most of them will be in the 250- to 500K. That's what -- you know, I would say that I -- I'm seeing in the market.

You know, most people are very comfortable going into a fund at 250-, and you're spreading that across 10 years. And that's -- that's not a whole lot across 10 years for most of those people that can afford that. So I would like to see the number increased. If we just said, okay, the average is 250,000 per -- you know, on -- on average, that's what accredited investors feel comfortable with and have been shown -- and I don't know that. I'm talking -- you know, that's what I see. But from the local funds here across the Midwest, you're looking at 600.

It would take 600 of them to get to 150 million. So I'm not saying that's the number. But I think we should increase the number. Otherwise, we're limiting the market again. We're putting limitations on the market.

MR. LEE: I agree, and I just -- I want to simplify kind of what I said earlier as well because I -- and Carla, thanks for organizing it that way. I think there is substantively two major issues. And to focus on what Catherine and Sapna is saying, you guys are talking about Series A equity rounds for growth-oriented companies, tech or otherwise.

In that case, venture capital exemption is absolutely the right strategy, and we can simply focus on VCOC, increasing, for example, to 150 million cap and, let's say, 500 -- making things up because, as we said, if we don't increase the 249, it doesn't change anything. Having said that, my other point was let's -- if we as a committee and the SEC believes what's also important is the underlying recipient of those dollars, the VCOC money is not going to go into small businesses that are typically not looking for capital appreciation; right?

These are all cash flow businesses. A fund manager who is compensated by the increase of their portfolio and their percentage, they are not going to be looking to invest in a business that might be profitable but not going to go 5X, 10X. Therefore, if the policy goes separate from the VCOC issue, it's to encourage investments in small businesses that are more cash-flow oriented, and predominantly almost all small businesses are. They are not tech companies.

In that case, if we want to leave the VCOC section alone, you have to look at the private fund exemption. And that also has to be looked at in the same context of we want to encourage number from 99 to, let's say, again, 500 as an example, and this is the point about qualified clients.

If you want to broaden the access, maybe there is a separate exemption that you don't have to be qualified clients. You can also only be accredited investors just like the accredited investors. So two separate topics, but hopefully that clears up what I was talking about.

MS. MOTT: Youngro, I like what you're saying because my point earlier was these -- you know, the funding post-Series A usually, you know, carries the company into being able to execute on, you know, one of three or four events. And that would be, as I said before to another Series B or in -- to the next round to strategic acquisition, which isn't necessarily always the most favorable option, and to a point where they can go to a bank and start borrowing money.

And at that point, you know, if it's a -- if it's going to be a viable entity and it's a -- you know, a growing lifestyle company, that's a point you can execute the provision to buy your shareholders out. You know, and they get the return. So you can write that into the documents early on.

You know, at five years, you X -- you achieve this amount in -- you know, in revenue. That -- at that point, we can trigger the option to, you know, buy us out. And everybody gets a -- you know, their -- their return on investment. So, I mean, it's a lot of -- I mean, it serves -- like you -- I like what you said. It serves a bigger market beyond the tech companies. I like that.

MR. YADLEY: I think the structure of the exemptions, it is confusing. But people are familiar with it. And I would not try and merge the two 3(c)(1) funds. Leave them as they are. I think our focus was on the qualifying venture capital fund. I was a little late coming back to lunch, so I don't know how we went from a hundred million before lunch to 150-, I mean, investor -- well, dollars.

Was there any magic to that or just trying to get a reasonable number? Either one, I think we should increase the number of beneficial owners. Again, back to my point earlier about diversification and being able to get more people involved.

And then I hope before we run out of time, we can talk about the ability to exclude from the exclusion fund-on-fund investments because I think Sapna and Catherine were both making pretty powerful arguments about flow of capital throughout the country on that.

MS. GARRETT: Okay. Thank you, Greg. I think -- let me summarize where I think we could be in terms of before we move on to the other point. So with respect to the qualifying venture capital fund exemption, we would recommend that the SEC increase the current $10 million limit up to $150 million.

I also heard that we'd like for the SEC to increase the number of beneficial owners that can invest in these funds. We didn't talk about a number there. The other thing I heard is that under the 3(c)(1) exemption under the general exemption that the SEC increased the number of accredited investors, which is currently 99, that could invest in these funds.

MS. WASHER: I mean, one idea would be to make it symmetrical and just say, in the generally tab, instead of less than a hundred, have it be less than 250. And then you keep the two prongs. I understand the concept of the two prongs, but at least they're parallel.

MR. SEATS: If they were parallel, though, then there is really no point in having the other -- I mean, the only -- as far as I can tell, the only reason for the qualifying venture capital fund structure to exist is to allow for a higher beneficial owner cap than the 3(c)(1) general. And so if they're aligned, then, like, no one will use that. It doesn't matter. Like you -- like -- and in effect, it is merging them because then you can get rid of the extra words in the reg; right?

MS. WASHER: Yeah. I didn't -- I never understood why it was a higher number of people that were allowed in the VC fund but only $10 million. I mean, that --

MR. SEATS: It certainly doesn't make sense. There's a reason why we're probably -- to push on things. I think you have to, like --

MS. WASHER: Yeah.

MR. SEATS: I think, like, philosophically, either there is a cap -- the number is higher or it doesn't make sense to exist because, in which case, you just go do a 3(c)(1) fund. You don't need this if you can -- you know, so -- but I'm getting -- I feel like we're getting coaching from Jeff that, like, maybe it's easier to suggest a change inside of this pocket that's already been identified for doing something more permissive. And if that's the case, then maybe we should live in that and just try to maximize --

MR. SOLOMON: Yeah.

MR. SEATS: -- what that looks like.

MR. SOLOMON: Yeah. I mean, my only coaching advice on this is just once you start messing with 3(c)(7) and 3(c)(1), it just -- it has a broader implication to other folks who use 3(c)(1) and 3(c)(7) exemptions that aren't venture funds. So Youngro's point is a good point. What about companies that aren't -- that wouldn't necessarily qualify as venture funds? That's a different issue we should address. I'm not sure that if qualified venture fund exemption is the right place to deal with it.

So my advice would be let's try to knock them into increments; right? Like we can't -- I think we run the risk of -- we try to boil the ocean here, we're going to end up running afoul of a bunch of different things. So there's a couple things we can solve for. As it relates to bringing venture money from the coast to the middle of the country and for -- to try to create a mechanism where we have onboarding or a financial incentive and a structural incentive for venture funds to finance local venture funds, two proposals. One -- and I would suggest we just -- let's just focus right now on the venture exclusion -- right? -- the venture fund exclusion for the time being. And so we can resolve that, and we can move on.

I think if we're all in agreement that we ought to shoot for a bigger number in terms of both the dollar amount and the number of investors, I think we can probably make a recommendation to the staff. Maybe we want to put $150 million number on that. And maybe we want to -- and say up to 500 investors as a starting point.

We can always say to the staff come back with your best recommendations. Our recommendation, it seems we should go to -- to try and see if we can have 150 million max and 500 investors for the very reasons that Catherine articulated, because you want people to -- write quarter-million-dollar checks. That’s going to be a critical part of this or $100,000 checks. And if you open up the aperture, both the number of investors as well as the size, you are likely to end up getting meaningful amounts of money raised, probably from the coast and that’s --

The third -- so that’s two recommendations. The third is the one that Sapna mentioned earlier, which is to exclude fund investments from the -- from the qualified bucket, meaning --

MR. SEATS: Include them to be defined as qualified, you mean? Include.

MR. SOLOMON: Hear me out. Hear me out for a second because we talked about this a little bit. If you include it as a qualified investment that is subject to the 20 percent cap -- so removing it means you can make it -- you can -- a hundred percent of your fund can be invested in venture funds. Right now, it’s part of the cap. So you’re permitted to make it. It’s just subject to the cap. So there is nothing precluding a qualified venture fund from making an investment in another fund right now. It just has to go into the

bucket.
MR. SEATS: What’s the definition of a qualified venture investment? It needs --
MR. LEE: You guys are talking about the same thing. Yeah. It’s a -- yeah. You are talking -- basically 80 percent -- 80 percent of the venture capital exemption has to be applied in investing qualified investments. So what Jason’s saying -- what, Jeff, you were saying as well is, like, including the fund definitions will, in fact --
MR. SEATS: That’s right. You have to expand the qualified definition to include that. That has to happen.
MR. SOLOMON: Yeah, yes.
MS. GARRETT: Right. Right.
MR. SOLOMON: So, yeah, you’re right. We are saying the same thing. We’re trying to get the -- well, we’re trying to get an investment in the fund outside of the -- outside of the 20 percent exemption.
MR. LEE: But if you’re going to -- so, Jeff, I actually agree with the framework. I think all of us, we’ve been around the block, understand how rules are made. So I do think it’s simpler to use a VCOC exemption as maybe the point. But -- and then exactly what Jeff said, number one, my suggestion would be to

make the qualifying number of investors to 600 because assuming the $250,000 is the right number, then that -- that's the max.

Six hundred investors, 250- is 150 million. And then the third category is to expand the definition of qualifying investments to include the type of investments Sapna talked about. My wholehearted recommendation was to include that, make that also include a type of small business investments. Maybe that's a business under $1 million of revenue or 5 million revenue. Maybe it's a -- how you want to define the small business angle because that will create incentives for individuals who want to invest in these companies to utilize an exemption to create a fund to, say, support local business fund in Chicago, in Houston, in Tulsa because right now, unless we change that, the VCOC exemption will only be used to invest in technology companies or high-growth companies. It will not be used to invest in small businesses and Main Street businesses.

MS. WASHER: Agree.

MR. SOLOMON: Okay. So there is no -- so I want to make sure that -- that as we're thinking about crafting these -- and again, what we'll do is we'll, you know, work on the final wording after but conceptually make a recommendation along those lines for the qualified venture funds or for the VCOC exemption around that. So it addresses the issues we just discussed. Is that -- does anybody have any -- anything more to say on that? Then we can try to address two other issues. One is the one that Youngro brought up, which is what if you're not a venture fund. I'm not sure what we're doing on that front. And then the second --

MR. LEE: Yeah, Jeff, what I'm saying is I -- what I said can be exactly your third problem. Like your third problem was to expand the definition of qualifying investments to include the fund investments. What I'm saying is you can also include the -- the small business target as part of the qualifying investment definitions. So I'm using your framework.

MR. SOLOMON: Okay. I'm okay with that, too. Is that -- everybody else okay with that?

MS. WASHER: Yeah.

MR. SEATS: How do you --

MR. SOLOMON: Okay.

MR. SEATS: -- define that, Youngro? Is it based on the definition of the small business size or --

MR. LEE: Yeah. That would be -- I love your -- everyone's recommendation because what we're talking about really is -- when we say invest all across the country, I assume we're not just talking about tech companies all across the country; right? We are talking about small businesses across the country. Like Jeff, your father used to work -- and Carla, your small businesses -- those are not tech companies, but we presumably want, you know, an easier way for fund managers to invest in those businesses.

So I would -- Jason, one example could be the size of the annual revenues -- right? -- whether it's, again, $5 million or less where, clearly, it's small businesses. Maybe it's the nature of the business. Maybe it's just debt; right? Like just include debt for small businesses. And that's --

MR. SEATS: Exploring it -- I think that that gets really tricky because defining it's going to be incredibly hard because if you try to do it by revenue, like, lots of venture-backed companies have no revenue for a long, long time; right? And so -- and what you'd be doing is, like, trying to carve in debt as a qualifying investment under that -- that rule set.

I don't have a problem with it. I just -- I just think that the coming up with a definition there is going to be -- like of all the things we're debating right here, that's going to be the hardest.

MR. LEE: I'll be -- for sure. And if that's the -- that's fine if we want to limit the change as the definition of VCOC to not meaning convoluted. That's totally fine. I am just pointing out that it will do nothing to increase investments in Main Street businesses.

MR. SOLOMON: But let's -- I mean, again, maybe there is another thing we can do here because I want to make sure we have some intangible --

MS. MEHTA: I think these are two separate issues.

MR. SOLOMON: Yeah. I think they are too, but one of the things -- I'd like the -- to understand from the staff is, like, look, the Small Business Investment Corporation, SBIC, stuff is meant to handle the companies that you're talking about; right? SBICs are meant to both -- from an equity standpoint and a debt standpoint, there is a bunch of incentive programs that's supposed to be able to get funding for small businesses. And there's a bunch of qualifiers on that.

And what I would suggest, I don't profess to know what those are. But I think there is already a regime in place for SBICs. And I'd like to understand before we make a recommendation -- I'd like to understand what the regime is that might be inhibiting SBICs from raising money to get it to the place you want to get it to.

Like I just -- I don’t know enough about it. So -- but I do know that there is the Small Business Administration, and SBIC licensure is a real thing. And there’s people who apply for it all the time, and they’re constantly raising 50 million, 75 million, $100 million to go to businesses that are not venture funds, that are not venture-oriented.

So maybe we could ask the staff to explore SBIC rules and understand if there’s some regulatory mechanism that’s inhibiting the flow of capital from -- inhibits people or makes it less likely for them to seek SBIC licensure. And I don’t know what that would be, but it seems to me that SBIC is -- that’s the -- that’s the rationale for SBICs to even be around. And I’m not sure why -- I don’t know enough about it yet to understand why that capital is not going the places where you think it should be going.

MS. GARRETT: So Jeff, I think that’s a good point. I do think we are running up against a little time constraint with the SBIC. And so Kesha, do you have comment on that?

MS. CASH: Yeah. And I know we’re running up against time, but I think Jeff’s point is a valid point. We’ve been sort of exploring SBIC, CRA. There are these pools of money that are out there that's designated for underserved communities that are essentially locked up by kind of old, old thought and old guard way of investing.

While we certainly need, you know, infrastructure and affordable housing, the SBIC, the CRA dollars, these dollars that are designated from communities we're talking about, they have -- they aren't being moved in probably the most innovative way. So I do think there's a big gap between what already exists and what could be the capital to support, you know, much of what we're talking about.

MS. GARRETT: Thank you. I agree with that. What I understand is that a lot of these are a lot smaller numbers and also would be very targeted to specific industries or loans. So I think there's a gap between that program and venture funds. So just to try to -- I like that, Kesha. Lots of paperwork. To -- Jeff, do you want to try to get us back on track with respect to -- I mean, should we move on a little bit to the venture capital advisory exemption and recommending that fund-of-fund investments be included in the qualifying investment definition and, therefore, not included in the 20 percent nonqualifying investment basket?

MR. LEE: I mean --
MS. GARRETT: Is that --
MR. LEE: One question. Is it possible -- Jeff, to your point, is it possible, without saying -- because what you said, that's hundred -- I'm a hundred percent supportive of that rule. But there is so many other cases. So if it's possible to at least generally frame it for the recommendation purposes to at least explore how to change or modify the definition of qualifying investments so that it will cover more the type of investments that we want money to go to. I think that could go a long way and would love if the opportunity presents for other experts or other industry members to present, like, what exactly are we talking about. What are they -- what kind of businesses -- like Kesha, like you would love to invest in under these exemption, but you can't because it's not a qualifying investment because I think there are so many different ways just by tweaking the number, the amount of category of qualifying investments, you can actually exponentially grow the type of investments going to local communities and small businesses.
A PARTICIPANT: I think we were --
MS. MEHTA: Sorry. I know we're running late, but what exactly is the type of investment that you

would want to invest in, but you find that you can't because of the nonqualifying definition?

MR. LEE: I think fundamentally, it will be debt. But Jason's point, it's very complicated. But fundamentally, I think it's debt-oriented investments because, for most small businesses, private fund managers like your funds will not be investing in the local bakery that needs half a million dollars loans; right? Like that -- it just doesn't work under those --

MR. SOLOMON: I got to tell you I think it's a giant can of worms. I get what you're saying so I'd like to split them in two. Like I -- you're going to get tremendous pushback from the direct lending community -- right? -- which is just -- you know, there's no reason for us to even bring that up when we can probably have a different discussion, which I think we should have. So maybe that's the second recommendation; right?

Let's ask the staff to explore other programs out there for lending -- right? -- broadly outside of the venture community, to explore that and maybe look at some of the -- some of the reasons why -- the causality. Why is -- are the -- are those programs not reaching the end markets that we know?

Just like -- listen. There was a lot of data presented today on a lot of the information that they're leading us to make these conclusions. We can say that, beyond venture, we can make it a part of the purview of the committee. I just don't want to muddy what we're already working on when we can probably come back over the next series of meetings and try to address things beyond venture, which I think is a good thing to say. So my recommendation, because we're getting short on time, my recommendation, just so -- and again, I'm not trying to force through something. I think we should focus on the venture -- the VC -- the venture exclusion. I think we should look at the dollar amount increase that we talked about, which is 150 million, and increase the number of investors. That addresses the venture -- the venture exclusion maybe creates a better pathway for venture funding.

Second, I think we can encourage or recommend that the staff come back with some thoughts on lending to small businesses and exploring the -- exploring the programs that are out there and ways we can make them more efficient from a capital formation standpoint for non-venture lending or for companies in general other than just looking at equity.

I am -- however the staff can come up with it helps us to frame the discussion, I don't want to limit it. I just want -- ask for vital input on other forms of capital that should be getting to these -- you know, to these companies that aren't for whatever reason.

MR. LEE: I agree with that, Jeff, and I do think that's the right way to think about it. It's not just lending, just to be clear. I would phrase it as non-equity investments. So it looks like -- explore non-equity investments that could be applicable to more type of businesses because I'm sorry to beat a dead horse, but if we don't change the definition of the qualified investments, the trend that we talked about earlier in the session, the difference between tech-oriented companies and Main Street businesses, it's going to get even larger. So I would definitely appreciate -- if other people agree, having a separate recommendation to explore non-equity investments and how the different exemptions could possibly support those.

MR. SOLOMON: Okay.

MS. GARRETT: And I think that the recommendation would not be for us to be voting on a recommendation to the Commission and to the SEC, but it was a recommendation just that we have the SEC staff -- you know, our staff here with us to help provide us more information in the future with respect to this information and so that we can become a little bit more knowledgeable about it for future meetings. And so it wouldn't be a recommendation that we're going to be voting on right now. It's just a topic that we would want to explore more in the future. Does that make sense, Youngro?

MR. YADLEY: That makes perfect sense.

MR. LEE: Hundred percent, yeah.

MS. GARRETT: Okay. So I think that we've identified three items to vote on, which we will now be repeating for the umpteenth time, but I'll do that so that we can vote.

With respect to the venture -- qualifying venture capital fund exemption from the Investment Company Act, the committee would recommend that the FCC increase the current 10 million limit up to $150 million.

The second thing would be that the SEC increase the number of beneficial owners under that exemption up to -- I heard 600 investors that could invest in these funds.

And the next one would be that the venture capital advisor exemption from the Investment Advisers Act that the committee recommends that fund-of-fund investments be included in the definition of qualifying investments and not included in the 20 percent nonqualifying investment basket.

And what -- we'll vote, but what I would also say is that everything that I just said, what we would do is polish these words up like we like to do, and we would also probably wrap some perspective around these and our recommendations.

We've had some really great comments from the committee members today about why we think that these are important for helping get money to underrepresented communities.

And I think that maybe in our specific recommendations, we're not addressing that. But we have addressed it in our committee meeting today. And so we want to tie these together with what we've heard earlier.

Based on that, did I say anything that anybody would like to change or say any differently?

Okay. Then I'd like to take a vote on all in favor of those -- presenting those three recommendations to the SEC. Please let me know -- can say -- all in favor, aye.

(Chorus of ayes.)

MS. GARRETT: Okay. And anybody opposed to those?

(No response.)

WRAP-UP AND ADJOURNMENT

MS. GARRETT: Okay. Great. Well, that was -- that was good. So thank you, everybody. I am very excited that we've made progress on these very important issues today, and I really hope that, you know, the SEC will listen to us and that this will help with getting capital to the underrepresented founders' community.

We will be communicating soon about dates for our future 2021 committee meetings.

I want to thank again the staff for all of your work, committee members for being here and doing everything that you do and the chair and the commissioners for participating in our meeting. And I hereby adjourn the meeting. Thanks.

(Whereupon, at 2:29 p.m., the meeting was adjourned.)

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PROOFREADER'S CERTIFICATE

In the Matter of: SMALL BUSINESS CAPITAL FORMATION ADVISORY COMMITTEE

Date: Friday, April 30, 2021

Location: Washington, D.C.

This is to certify that I, Christine Boyce, 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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Proofreader's Name) (Date)

REPORTER'S CERTIFICATE

I, Peter Shonerd, reporter, hereby certify that the foregoing transcript of 143 pages is a complete, true and accurate transcript of the meeting indicated, held on 4-30-21, at Washington, D.C. in the matter of: SMALL BUSINESS CAPITAL FORMATION ADVISORY COMMITTEE MEETING.

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

5-6-2021