

The background of the entire page is an abstract, artistic composition. It features a dense arrangement of overlapping, translucent, circular and oval shapes in shades of deep blue, magenta, and purple. These shapes have a glass-like or liquid-like texture, with some appearing as if they are part of a larger, complex structure. A prominent glass dropper, with a clear bulb and a long, thin tube, is positioned diagonally across the left side of the image. The tip of the dropper is pointing towards the center, and a small, clear droplet is suspended just above it. The lighting is dramatic, with bright highlights and deep shadows, creating a sense of depth and movement. The overall effect is a visually striking and modern aesthetic.

ANNUAL REPORT FOR FISCAL YEAR 2021

Office of the Advocate for Small Business Capital Formation

U.S. SECURITIES AND EXCHANGE COMMISSION

ABOUT THIS REPORT + ACKNOWLEDGEMENTS

This annual report of the Office of the Advocate for Small Business Capital Formation for Fiscal Year 2021 is being delivered to the Committee on Banking, Housing, and Urban Affairs of the U.S. Senate and the Committee on Financial Services of the U.S. House of Representatives in accordance with Section 4(j) of the Securities Exchange Act of 1934 (the Exchange Act), as amended by the SEC Small Business Advocate Act of 2016, 15 U.S.C. § 78d(j)(6).

Pursuant to Section 4(j)(6)(D) of the Exchange Act, this Report is provided directly to the committees of Congress without any prior review or comment from the Commission, any commissioner, any other officer or employee of the Commission, or the Office of Management and Budget. It does not necessarily reflect the views of the Commission, the Commissioners, or staff of the Commission.

The work of the Office is possible only through the support of our talented and passionate colleagues across the agency. The Office owes special thanks to our colleagues who provided resources for this Report, including the Division of Economic and Risk Analysis for providing data to quantify the state of small business capital formation and contextualize issues, and the Office of Public Affairs for making our written product for this report visually engaging. We particularly thank the following individuals: Daniel Bresler, Vladimir Ivanov, Andy Kim, Angela Huang, Olga Itenberg, Rey-Er Lee, Wei Liu, Richard Oliver, Chris Onrubia, Zehra Sikandar, and Huaiqiang (John) Zheng.

Message from the Advocate



This has been a year of challenges as well as growth for so many in the capital raising ecosystem. Arguably the entire world paid more attention to the intricacies of innovation than ever before, listening to every update on vaccine trials, approval processes, manufacturing scale, and distribution logistics. We all had a proverbial magnifying glass in hand, examining innovation at each step of the way. It is for that reason that the visual theme of this year's report is "innovation up close," presenting an up close view of the intricacies of the technologies, developments, and growth happening around us thanks to entrepreneurs and investors working together.

More broadly, in 2021 we saw the increased attention on racial equity creating ripple effects in capital formation; however, much more work remains. The past year was also a banner year for capital raising, whether looking at the venture capital dollars invested into growth companies, the exit activity of later stage companies into the public markets, or the reinvestment of investors' returns put back into new funds that will support the companies of tomorrow. However, those headlines only tell part of the story: that of the companies who beat the odds and make the headlines. For every one of those, there are countless other entrepreneurs who are struggling to navigate the inside baseball world of capital raising, to bridge outside of their personal networks to sophisticated investors, to build a first-time fund in the middle of the country, or to determine which exit path makes the most sense for their company. We are acutely aware of the challenges these entrepreneurs face, staring at a system that holds promise trapped behind closed doors.

In 2021 we were thrilled to collaborate with Chair Gensler and Commissioners Peirce, Roisman, Lee, and Crenshaw on outreach events and policy matters. Looking ahead to 2022, we will continue to advocate for solutions to improve the capital raising opportunities for the dreamers, builders, doers, creators, and investors who you don't see in the headlines today, but whose names we hope you read about in the future. We look forward to collaborating with Congress, the Commission, and our many partners on pragmatic solutions to improve the capital raising ecosystem for all.

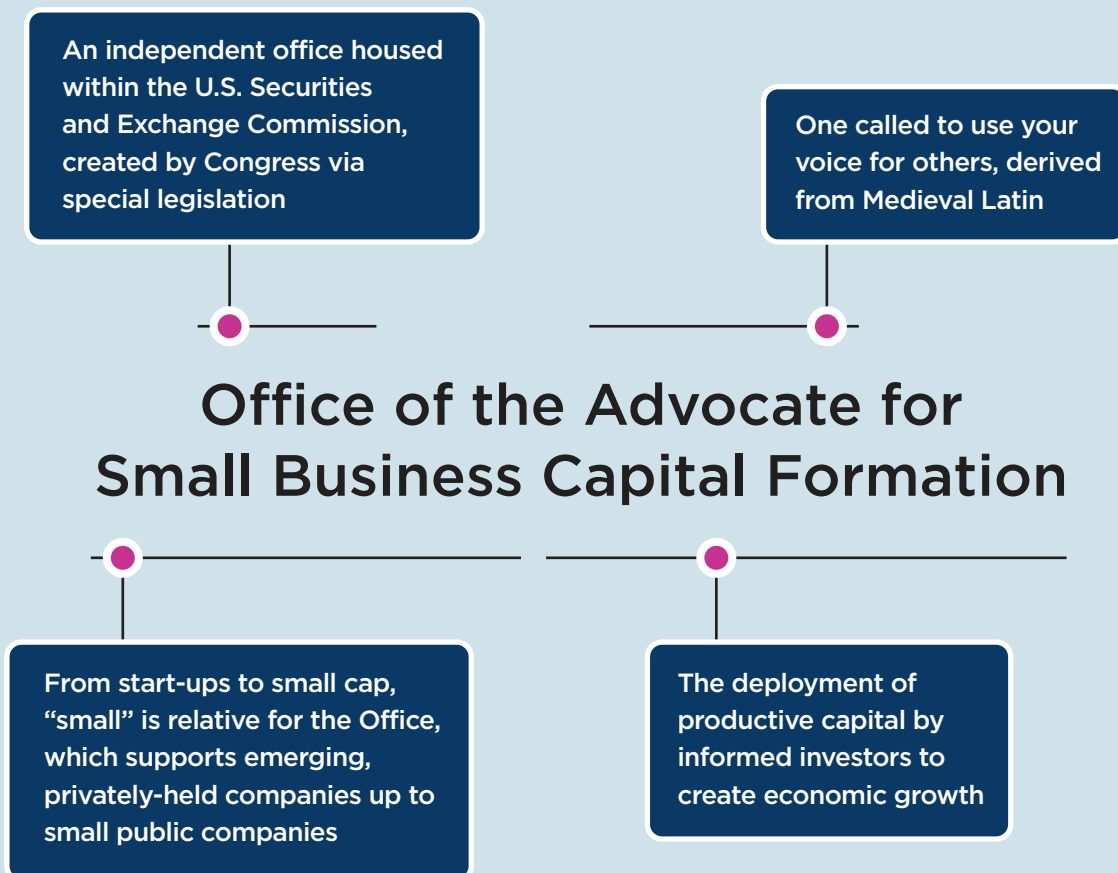
Finally, to the readers of this report, I want to say thank you. Thank you for caring about the opportunities for entrepreneurs to partner with investors to bring innovations to market. Your commitment to supporting capital raising opportunities is what makes our team's advocacy work so impactful, and we are grateful for your partnership and support.

A handwritten signature in black ink that reads "Martha Legg Miller". The signature is written in a cursive, flowing style.

MARTHA LEGG MILLER

Director
Office of the Advocate for Small Business
Capital Formation

Breaking Down Our Long Title



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About the Office

The Office advocates for solutions to address challenges faced by small businesses and their investors raising and deploying capital. “Small business” for the Office spans from early-stage start-ups raising seed capital, to later-stage private companies whose founders and investors are seeking liquidity in the public markets, all the way to smaller public companies. Congress established the Office via the bipartisan [SEC Small Business Advocate Act of 2016](#) as an independent office within the U.S. Securities and Exchange Commission (SEC) that reports to the entire Commission as well as to multiple committees of Congress.

The Office approaches its advocacy mission by:

- Engaging with small businesses and their investors to understand their most pressing capital raising issues;
- Identifying unique capital raising challenges faced by minority-owned, women-owned, rural, and natural disaster-affected small businesses and their investors;
- Analyzing the potential impact of policy changes likely to significantly affect small businesses and their investors; and
- Advocating to Congress and the Commission for policy changes.

Mission

We champion pragmatic solutions so that small businesses—from startups to smaller public companies—and their investors can build great companies together using our capital markets.

Core Values

- **ACCESSIBILITY** — We engage with both small businesses and their investors, as well as with the SEC, SROs, Congress, and other agencies on a regular basis through a variety of channels.
- **INCLUSIVITY** — We encourage people to speak openly and contribute authentically to facilitate greater trust and collaboration.
- **PRAGMATISM** — We approach problems with a solution-oriented mindset to make practical recommendations.
- **EFFICIENCY** — We operate like a lean start-up, maximizing resources and focusing activities where the Office can have a meaningful impact.

Our Advocacy Team



MARTHA LEGG
MILLER
Director



SEBASTIAN GOMEZ
ABERO
Deputy Director



COLIN A. CALEB
Attorney



JENNY J. CHOI
Special Counsel



JULIE ZELMAN
DAVIS
Senior Special Counsel



SARAH R. KENYON
Capital Formation Analyst



JESSICA W.
MCKINNEY
Special Counsel



AMY REISCHAUER
*Strategic Engagement
Advisor*



JENNY RIEGEL
Policy Manager



MALIKA SULLIVAN
Executive Assistant



TODD VANLAERE
Law Clerk

Strategic Plan for 2021-2025

Earlier this year, our Office developed a [2021-2025 Strategic Plan](#) to guide our team's decisions and align actions with mission execution. The Office made the plan publicly available in furtherance of our core values, outlining four key goals, with strategies and initiatives underpinning each. A summary of the contents of the strategic plan is included below:



GOAL 1

Engage with small businesses and their investors to solicit views on relevant capital raising issues.

Strategy 1.1: Conduct outreach with diverse audiences.

Strategy 1.2: Host the SEC's annual Small Business Forum.



GOAL 2

Educate small businesses and their investors about capital raising rules to reduce barriers to entry and increase compliance.

Strategy 2.1: Develop accessible educational materials about capital raising.

Strategy 2.2: Optimize content and delivery based upon changes in market needs and preferences.



GOAL 3

Collaborate on pragmatic policy solutions to address capital raising challenges faced by small businesses and their investors.

Strategy 3.1: Assist small businesses and their investors in resolving issues encountered with the SEC or self-regulatory organizations (SRO).

Strategy 3.2: Analyze data on capital raising to identify trends and gaps in funding, including for underrepresented and rural founders, and in areas affected by natural disasters.

Strategy 3.3: Promote practical policy solutions for Commission or Congressional action to address capital raising challenges.

Strategy 3.4: Deliver annual reports to Congress and the Commission that advocate for capital raising solutions.

Strategy 3.5: Support the SEC's Small Business Capital Formation Advisory Committee in providing advice to the Commission on capital raising policy.



GOAL 4

Empower a mission-driven team to leverage varied perspectives to solve the complex problems of an evolving and increasingly diverse capital market.

Strategy 4.1: Advance diversity, equity, and inclusion (DE&I) throughout Office operations.

Strategy 4.2: Foster a culture of connectivity, collegiality, and collaboration among Office staff.

Highlights from FY2021

While we look forward to the day we can gather safely in person, we have continued to seek opportunities to engage with diverse audiences across the small business ecosystem through virtual events and speaking engagements to share information about our Office's products, programs, and services and to hear from small businesses, their investors, and other thought leaders in the market. Some of the events in which we have engaged this year include:





Presented at Kenan Institute's Frontiers of Entrepreneurship Conference on unique challenges facing entrepreneurs from diverse backgrounds in accessing resources, expertise, and funding.



Partnered with our New York and San Francisco regional offices on a multi-panel event focusing on Tech Entrepreneurs of Color: Taking the Pulse of Capital Raising in New York and California.



Led the SEC's 40th annual Small Business Forum over four days, featuring the topics Finding Your First Dollars, Doing Your Diligence, Diversifying Capital Allocators, and Small Cap Insights.



Spoke at the Women of Color and Capital Conference, convening diverse women entrepreneurs and professionals to learn about money, finance, capital, and investing.

Televised interview with Faith Bautista of the National Diversity Coalition on *Spectrum TV: Owning a Piece of America*, focusing on access to capital and small business creation in low-and moderate-income and minority communities in Southern California.



Hosted a Spanish-language "charla" event with the University of Puerto Rico and local entrepreneurs and investors to share educational resources and learn about capital raising challenges.



Joined the SEC's Office of Minority and Women Inclusion and Office of Investor Education and Advocacy to share resources with the Minority Business Development Agency's Enterprising Women of Color program.

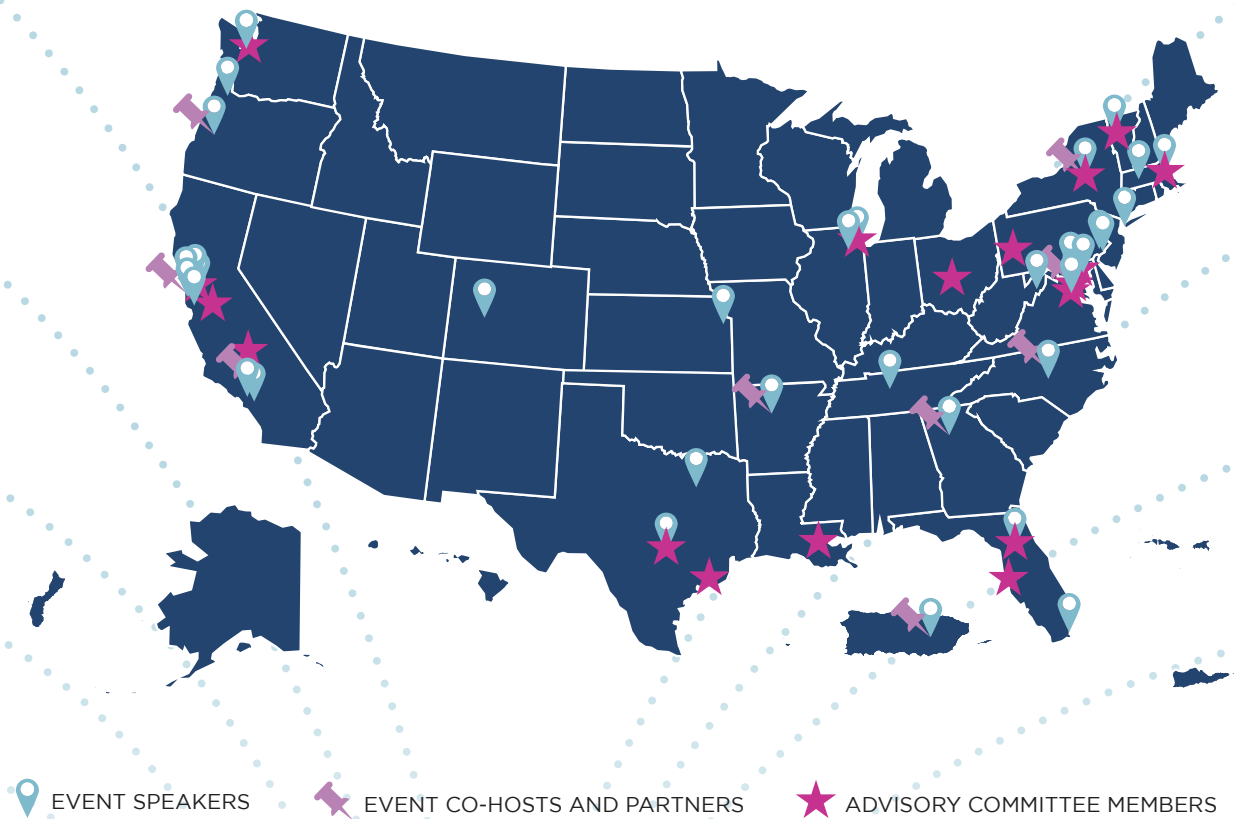


Q3 FY2021

Q4 FY2021

Outreach and Engagement

Through our outreach events, we engage with small businesses and their investors from around the country to hear their perspectives on issues facing the small business ecosystem, from regulatory policy, to changing trends in capital raising, to unique challenges and opportunities of demographic groups and different geographic regions. The insight we gain at our public events from small business ecosystem participants provides timely, practical feedback to inform the Commission's policymaking.



Our outreach engages speakers and audiences from

coast to coast.

40th Small Business Forum

The SEC's annual [Small Business Forum](#) is a unique event where members of the public and private sectors gather to provide feedback to improve capital raising policy.¹ The Forum covers a broad range of issues affecting small businesses and their investors, from early-stage entrepreneurial ventures to smaller public companies.

This year marked the 40th Forum, which the Office hosted virtually over four days from May 24 to May 27, 2021. Each day featured a different topic, with speakers highlighting success stories, as well as areas for policy improvement. At the end of each day's session, participants prioritized policy recommendations on that topic to be submitted to the SEC and to Congress. Video archives of each day's events are available in the [Forum video gallery](#).

Monday, May 24

Finding Your First Dollars

Navigating Your Way to
Raise Early Rounds



Tuesday, May 25

Doing Your Diligence

How Savvy Early-Stage Investors
Build Diversified Portfolios



Wednesday, May 26

Diversifying Capital Allocators

Tools for Emerging and Smaller
Funds and Their Managers



Thursday, May 27

Small Cap Insights

Perspectives on Smaller
Public Companies



On September 27, 2021, the Office delivered the [2021 Forum Report](#) to Congress, which summarizes the Forum proceedings, including the recommendations developed by participants for changes needed to the capital raising framework and the Commission's responses to the recommendations.

Educational Content

We hear from many people in the small business ecosystem struggling to navigate the complex capital raising framework.² As part of our efforts to make pathways to raising capital more accessible to small businesses and their investors, we have developed a number of digital resources.

Cutting Through the Jargon

This year, we launched a curated [glossary](#) of key terminology used in capital raising, from seed capital through later-stage deals. The full glossary is on the new [Capital Raising hub](#) online, with a few highlighted terms below.

Dilution

[noun] | dih-loo-shuhn |

Dilution occurs when a company issues new shares of *stock*, leaving the existing stockholders with a smaller percentage ownership interest in the company.

Diversification

[noun] | duh-vur-suh-fuh-kay-shuhn |

Diversification is an investment strategy to reduce the impact of any single loss by allocating investments across multiple asset classes, categories, or companies. Investors in early-stage companies often use portfolio diversification, whether through *pooled investment vehicles* or as an individual *angel investor*.

Liquidity

[noun] | li-kwid-i-tee |

Liquidity refers to how easily or quickly a security can be bought or sold in a *secondary market* without significantly impacting its trading price.

Securities of private companies are generally illiquid assets because there are typically fewer buyers and sellers, and resale restrictions pursuant to *Securities Act* Rule 144 may apply to securities acquired in an *exempt offering*.

Portfolio Company

[noun] | pawrt-foh-lee-oh kuhm-puh-nee |

A portfolio company is an operating company that has received an investment from a fund. A portfolio company generally represents one of several investments for a fund (for example, a *venture capital fund* or a *private equity fund*).

Series Round

[noun] | seer-eez round |

Companies typically raise money from investors in a series of *funding rounds*, in which investors, often including *venture capital funds*, provide money in exchange for *preferred stock*.

Series rounds may also be broken into early-stage (Series A and B) and late-stage (Series C+). While the use of proceeds varies, commonly:

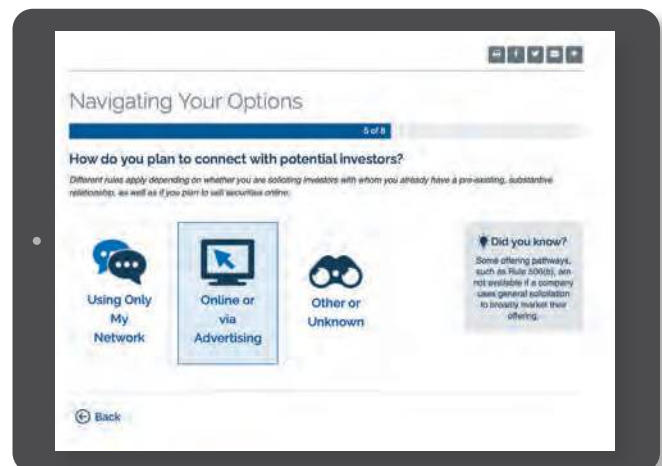
- (1) Series A often supports a company with an initial customer base and proof of concept.
- (2) Series B often supports a company scaling production and expanding customer base.
- (3) Series C often supports companies optimizing operations in preparation of a future initial public offering.

Interactive Tools on the New Capital Raising Hub



We recently launched a new suite of content for entrepreneurs and their investors on sec.gov/capitalraising.

The interactive [Navigator](#) is designed to help users narrow down their options for how to raise capital based on their expressed needs.



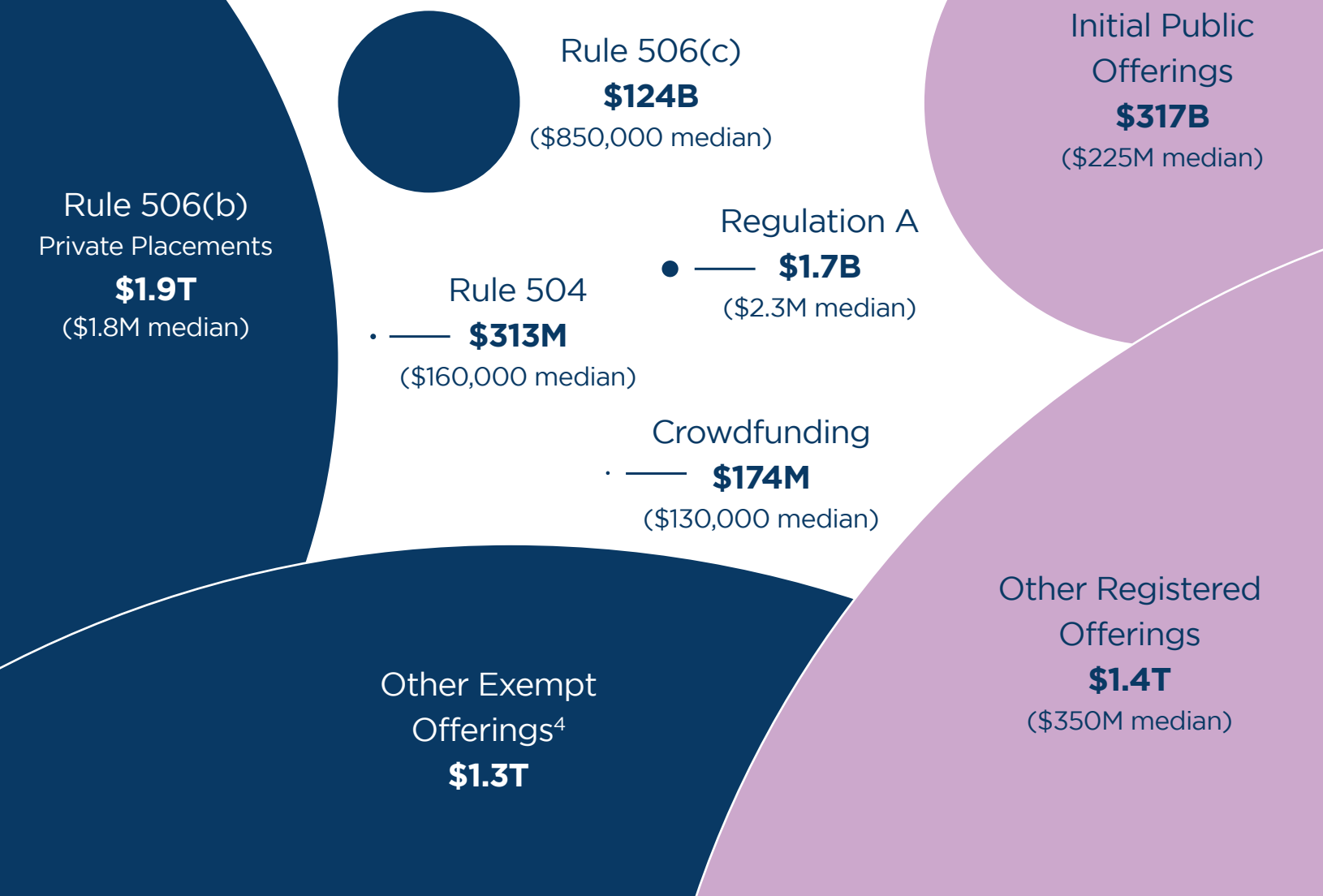
The [Capital Trends](#) maps allow users to engage with data on where capital is being raised across the country.



State of Small Business Capital Formation

The data provided in this Report is derived from a combination of public filings with the SEC, as analyzed by the SEC's Division of Economic and Risk Analysis (DERA), and is supplemented with figures and findings from third parties. In doing so, we hope to provide a snapshot view of the state of U.S. small business capital formation, amalgamating many important pieces of the capital formation story into one resource to aid in evaluating the current flow of investment capital between small businesses and investors. The data supplements anecdotal evidence and helps quantify the successes and challenges in small business capital formation nationwide. Unless otherwise indicated, the data period utilized for DERA data is July 1, 2020 to June 30, 2021. Using data, we can better identify what tools, strategies, and approaches would be most helpful in crafting policy solutions.



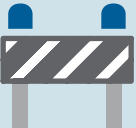


What regulatory pathways are companies using to raise capital?³



What pathways are available to raise capital from investors?

EXEMPT OFFERINGS

Offerings conducted pursuant to an exemption from registration are often referred to as exempt offerings. There are multiple exemptions available for small businesses looking to raise capital from investors.

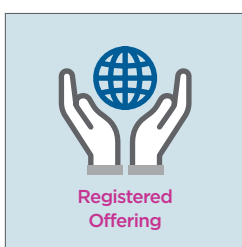
 <p>Rule 506(b) Private Placements</p>	<p>Rule 506(b) Private Placements allow companies to raise unlimited capital from investors with whom the company has a relationship and who meet certain wealth thresholds or have certain professional credentials. A company cannot use general solicitation in a 506(b) private placement.⁵</p>
 <p>Rule 506(c) General Solicitation Offerings</p>	<p>Rule 506(c) General Solicitation Offerings allow companies to raise unlimited capital by broadly soliciting investors who meet certain wealth thresholds or have certain professional credentials.⁶</p>
 <p>Rule 504 Limited Offerings</p>	<p>Rule 504 Limited Offerings allow companies to raise up to \$10 million in a 12-month period, in many cases from investors with whom the company has a relationship.⁷</p>
 <p>Regulation Crowdfunding</p>	<p>Regulation Crowdfunding Offerings allow eligible companies to raise up to \$5 million in investment capital in a 12-month period from investors online via a registered funding portal.⁸</p>
 <p>Intrastate Offerings</p>	<p>Intrastate Offerings allow companies to raise capital within a single state according to state law. Many states limit the offering to between \$1 million to \$5 million in a 12-month period.⁹</p>



Regulation A Offerings (sometimes called a "mini-IPO") allow eligible companies to raise up to \$20 million in a 12-month period in a Tier 1 offering and up to \$75 million in a 12-month period in a Tier 2 offering through a process similar to, but less extensive than, a registered offering.¹⁰

REGISTERED PUBLIC OFFERINGS

A registered public offering is commonly used to describe an offer and sale of securities that has been registered under the Securities Act. Companies must file a registration statement with the SEC and may not sell the securities until the SEC declares the registration statement effective.



Registered Offerings allow companies to raise unlimited capital through initial public offerings or secondary offerings using a registration statement filed with the SEC.¹¹



Initial Public Offerings provide an initial pathway for companies to raise unlimited capital from the general public through a registered offering. After its IPO, the company will be a public company with ongoing public reporting requirements.¹²

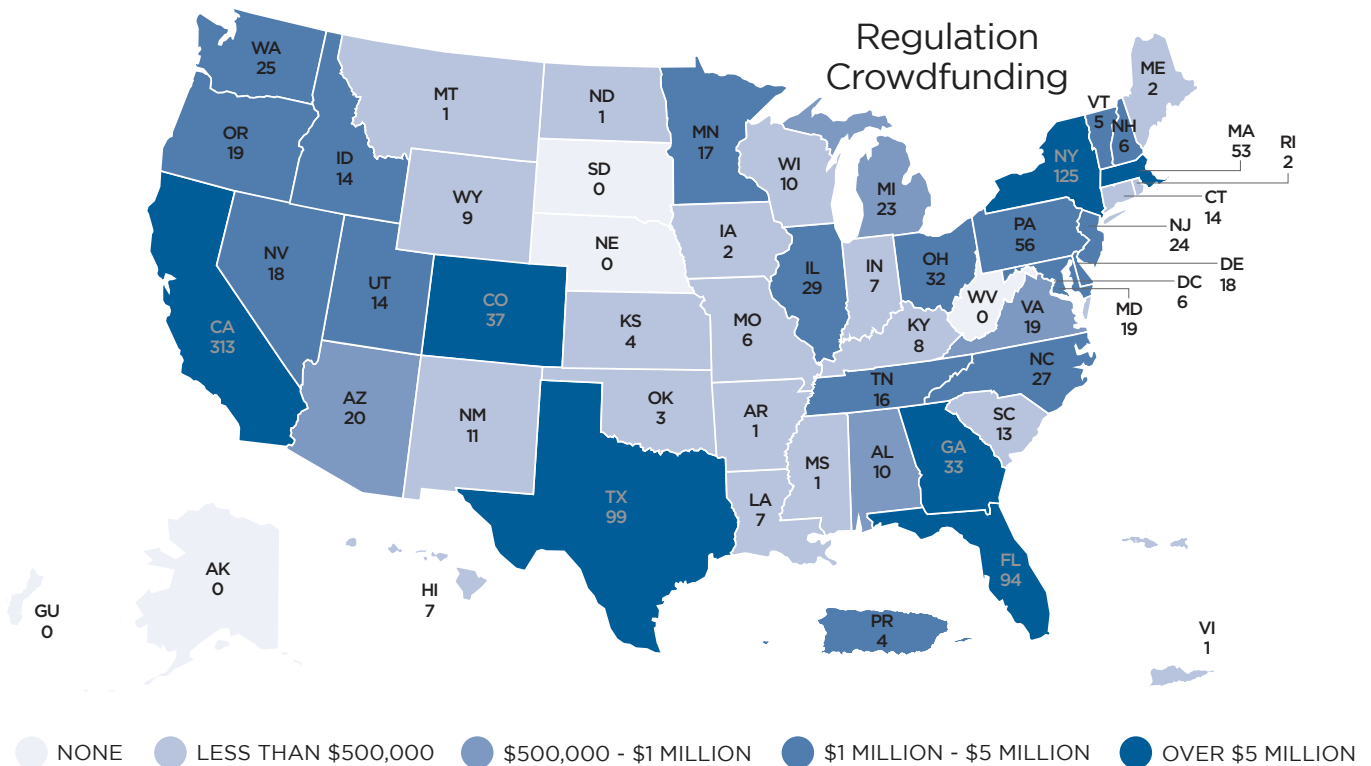
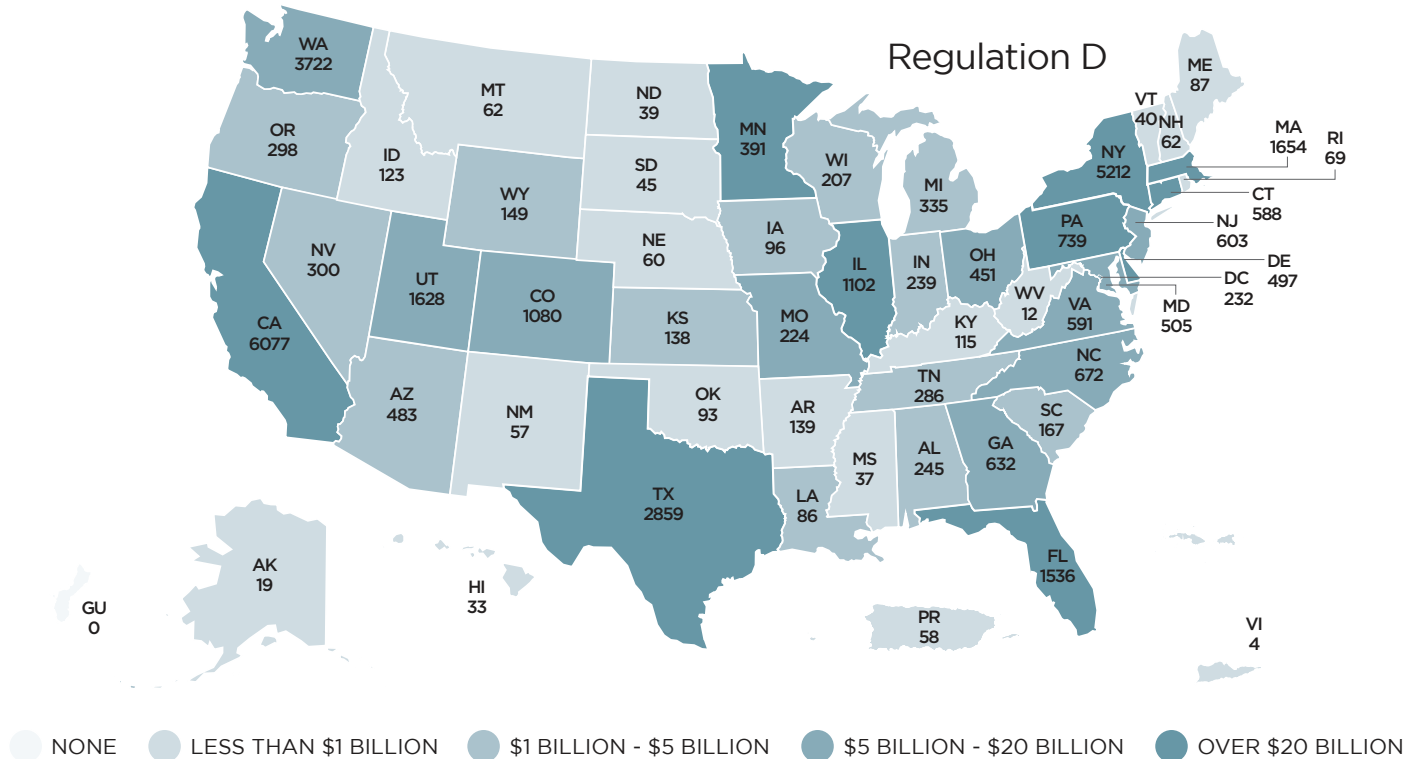


In a stable world, it's best to be data-driven. In a changing world, it's better to be data-informed. Data can reveal patterns from the past. It takes judgment to predict how those patterns will evolve in the future. Data shouldn't guide decisions. They should inform decisions.

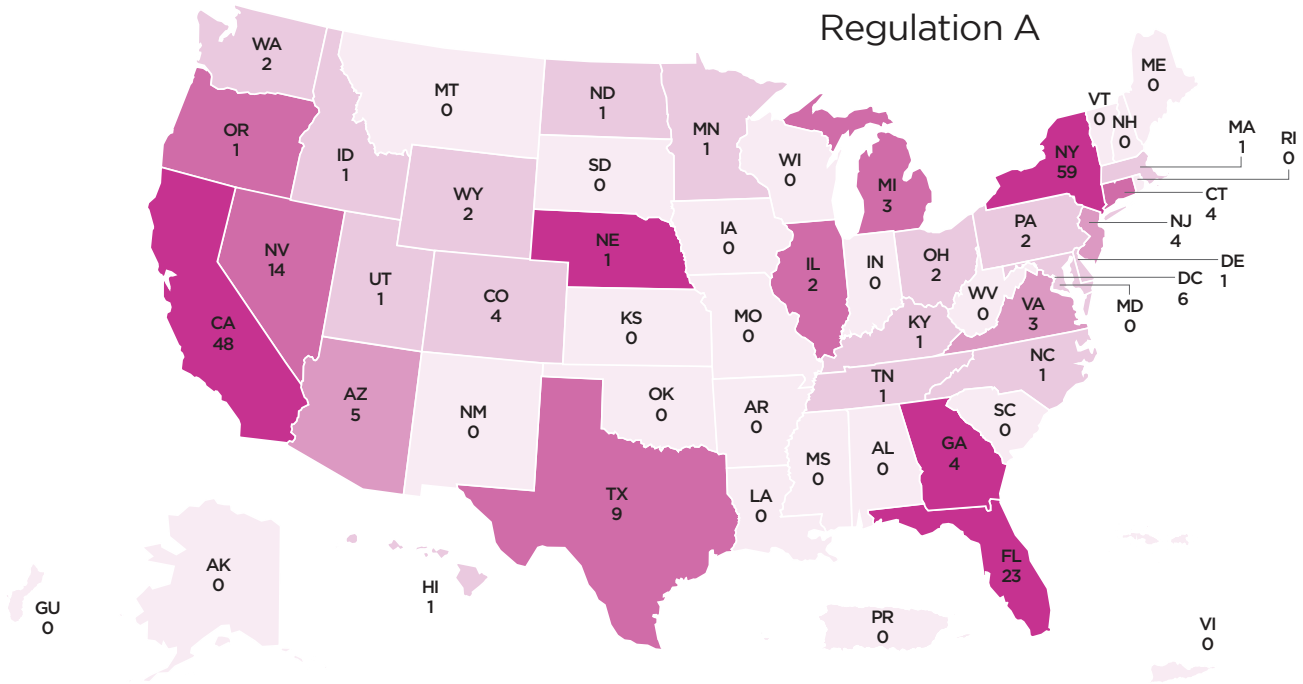
ADAM GRANT¹³

Where are companies raising capital?¹⁴

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

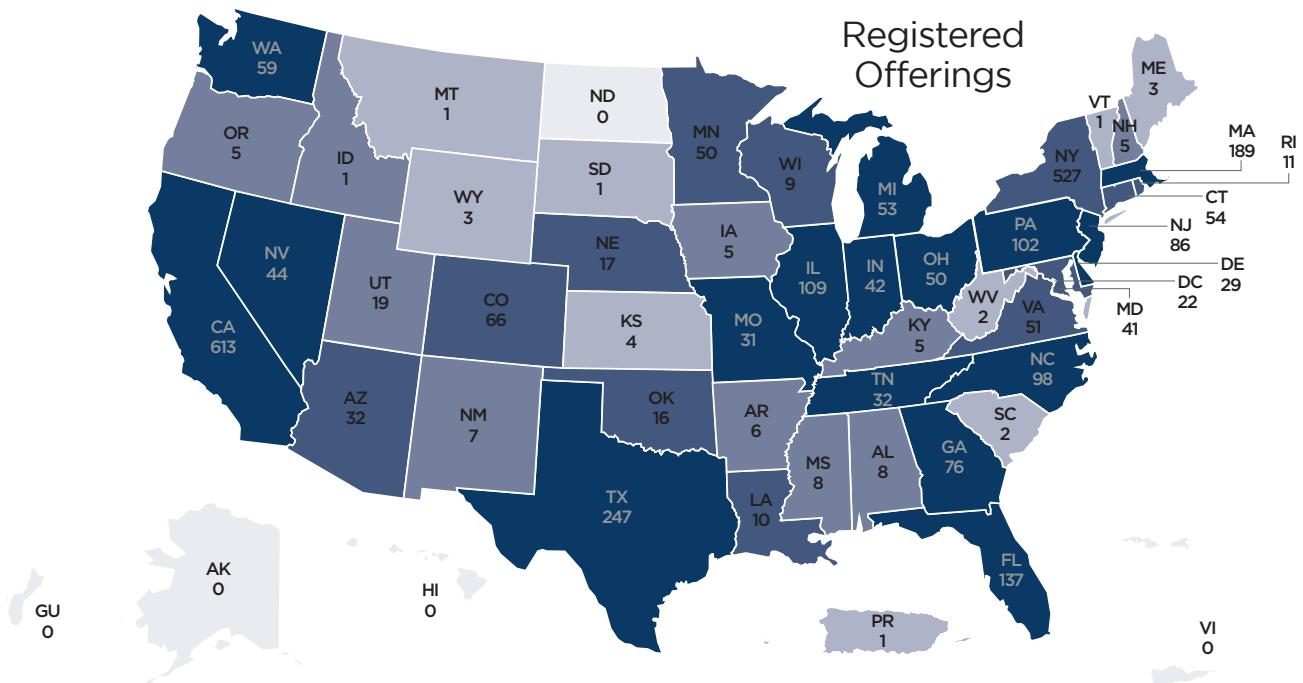


Regulation A



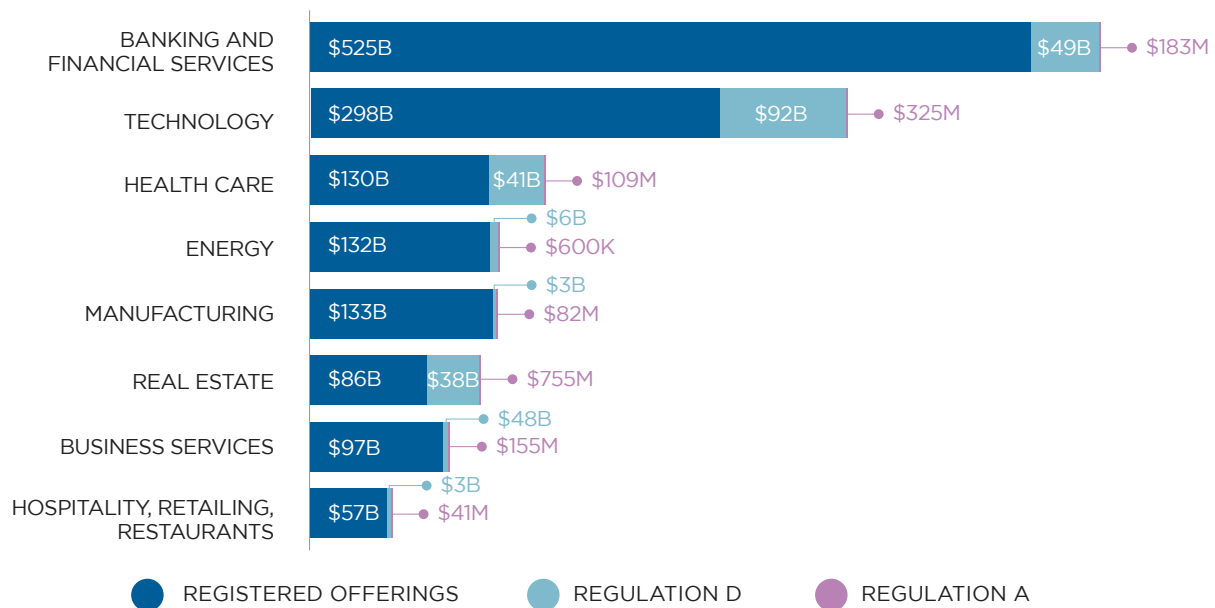
NONE
 LESS THAN \$5 MILLION
 \$5 MILLION - \$20 MILLION
 \$20 MILLION - \$75 MILLION
 OVER \$75 MILLION

Registered Offerings



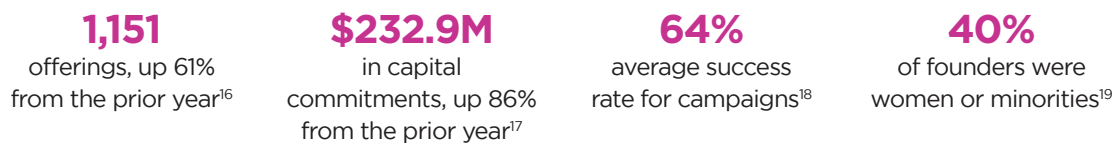
NONE
 LESS THAN \$1 BILLION
 \$1 BILLION - \$5 BILLION
 \$5 BILLION - \$20 BILLION
 OVER \$20 BILLION

How are different industries using the top 3 offering pathways to raise capital (excluding pooled funds)?¹⁵

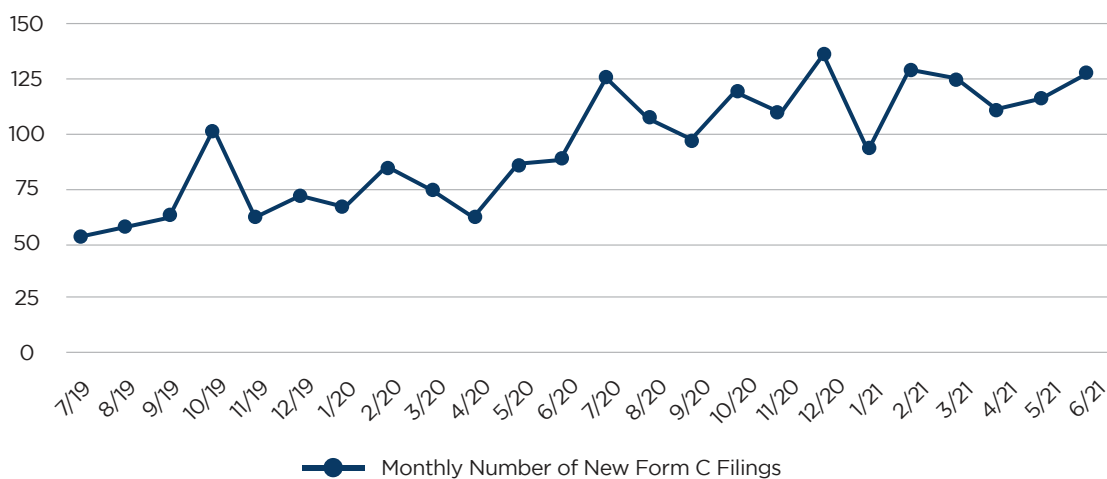


What is happening in Regulation Crowdfunding?

2020 was a record year for crowdfunding.

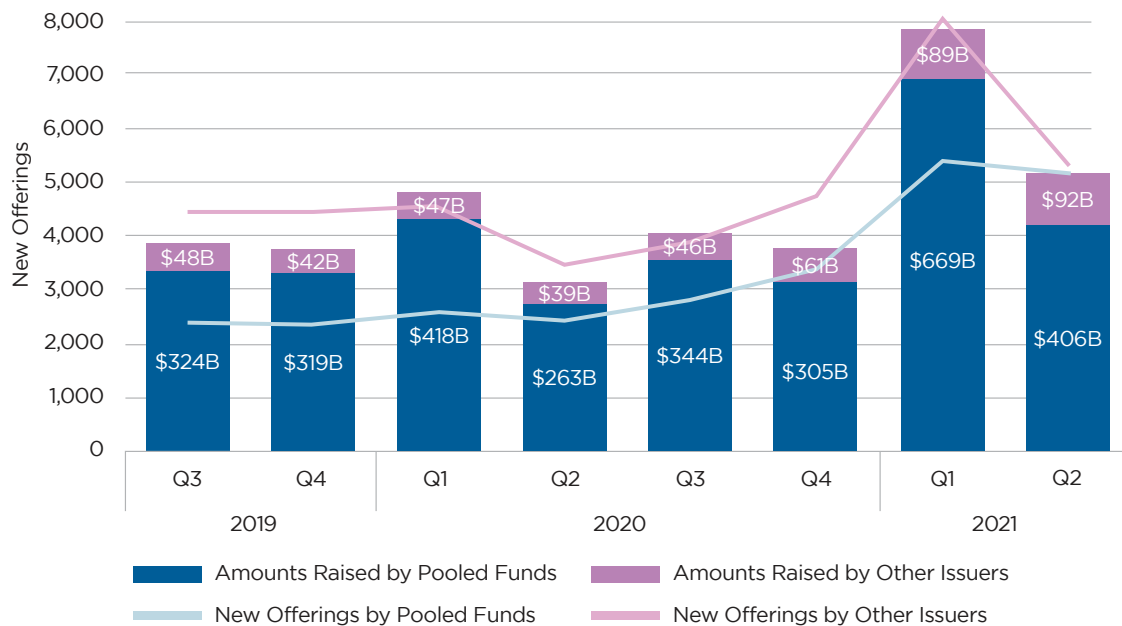


The number of crowdfunding offerings has increased over time.²⁰

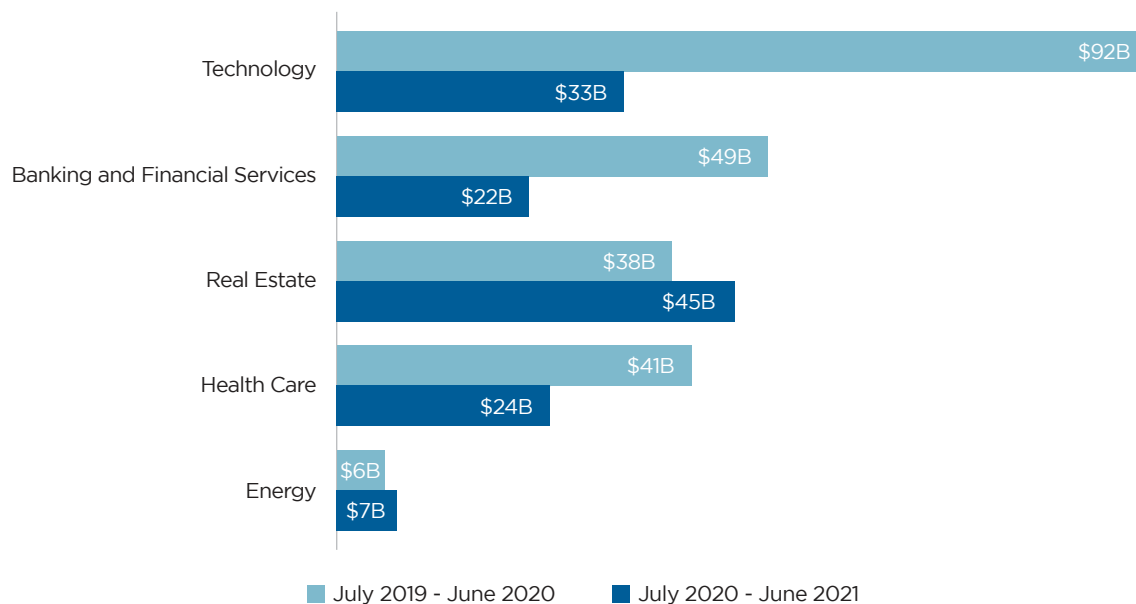


What is happening with Regulation D offerings?

Pooled funds continue to be the dominant users of Regulation D.²¹

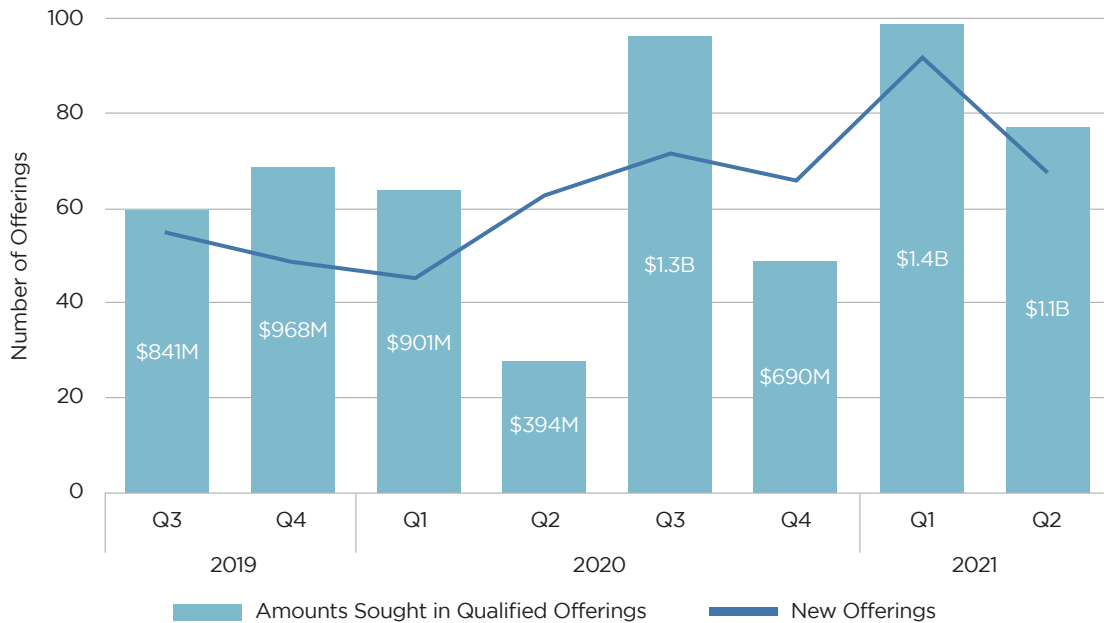


What are the top industries raising capital through Regulation D (excluding pooled funds)?²²

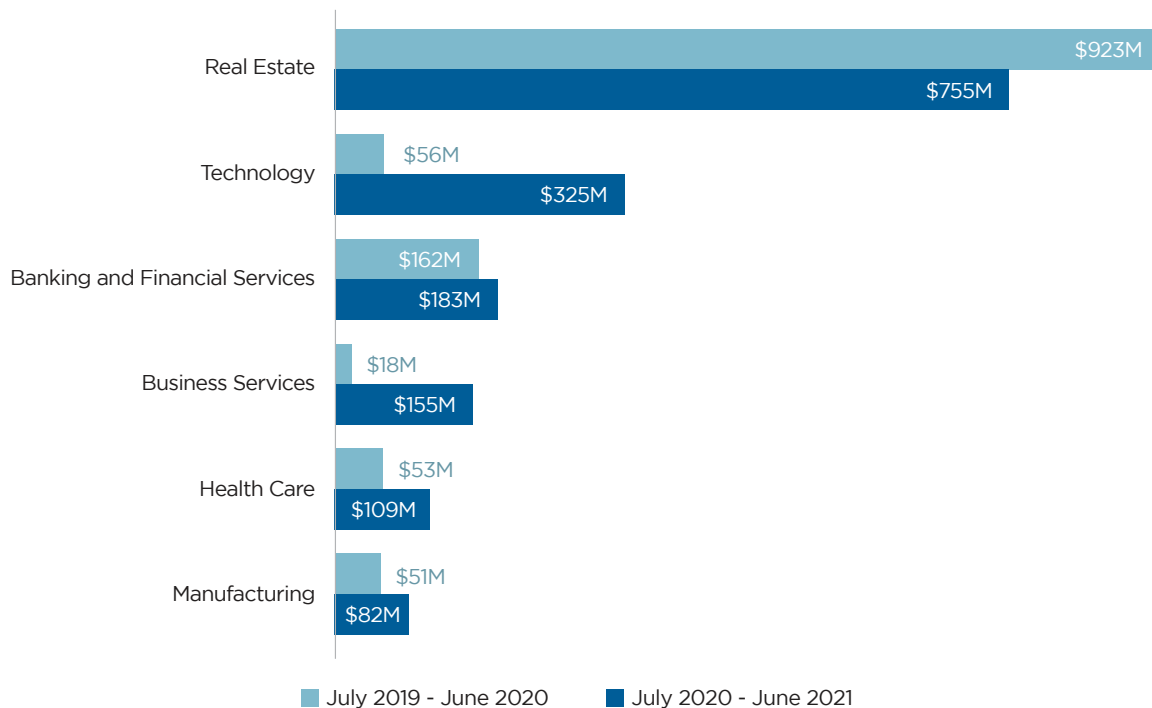


What is happening with Regulation A offerings?

Though variable across quarters, the number of offerings and amounts sought have continued to climb.²³

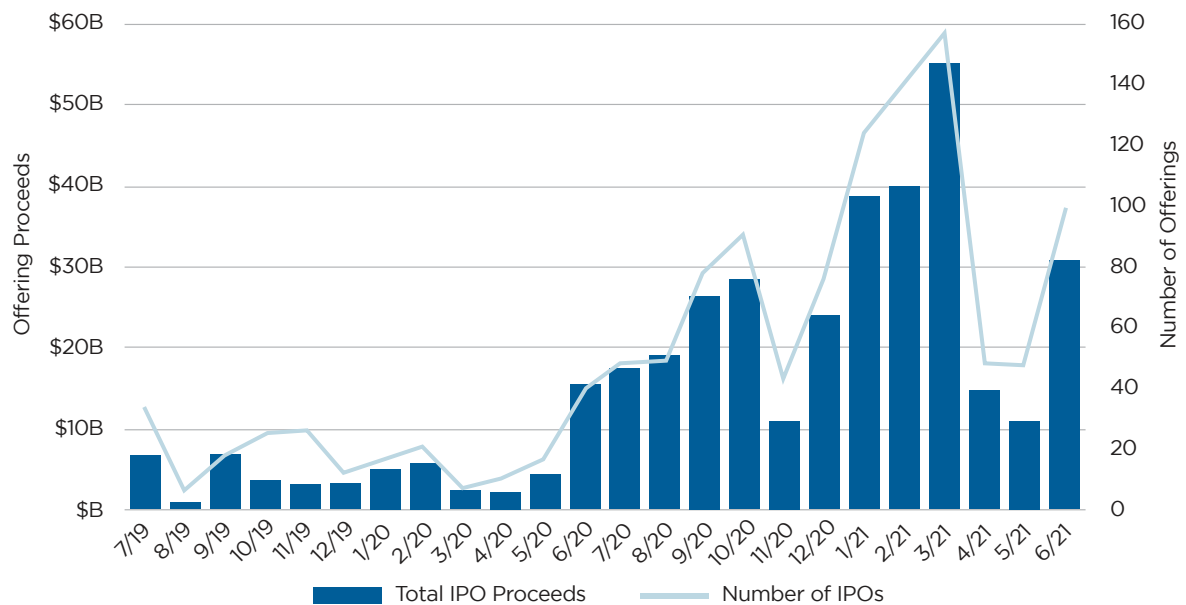


What are the top industries seeking capital through Regulation A?²⁴



What is happening with IPO activity?

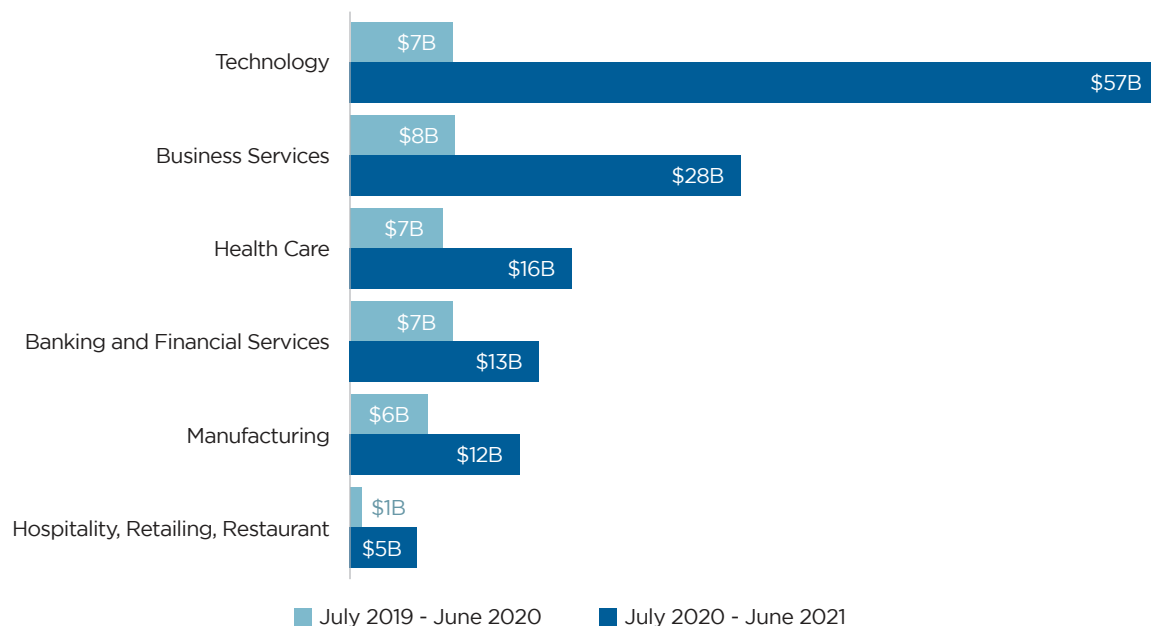
2020 and the beginning of 2021 saw a marked increase in IPO activity.²⁵



How does the past year's IPO activity compare to the year prior (excluding pooled funds)?²⁶



What are the top industries raising capital in IPOs (excluding pooled funds)?²⁷

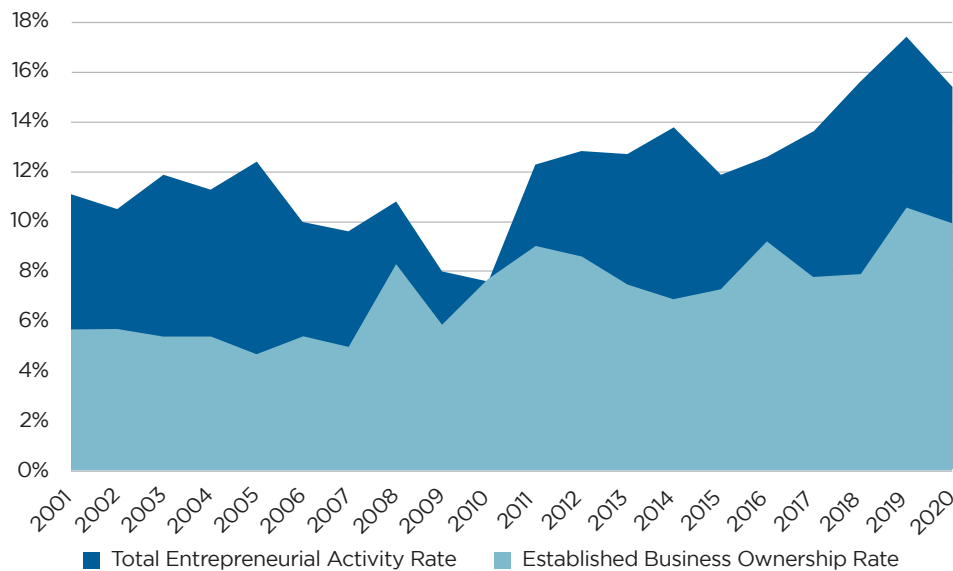


Small and Emerging Businesses

This segment of companies includes both high-growth startups that raise capital to get off the ground and launch early prototypes, as well as small businesses that create local jobs but may not fit the high-growth model that is the typical target of venture capital (VC) investments.²⁸

Entrepreneurship rates dipped in 2020 in response to the COVID-19 pandemic

While many press stories have featured entrepreneurs creating new businesses out of necessity or newfound opportunity in response to COVID-19, both the total entrepreneurial activity rate and the established business ownership rates dipped in 2020.²⁹

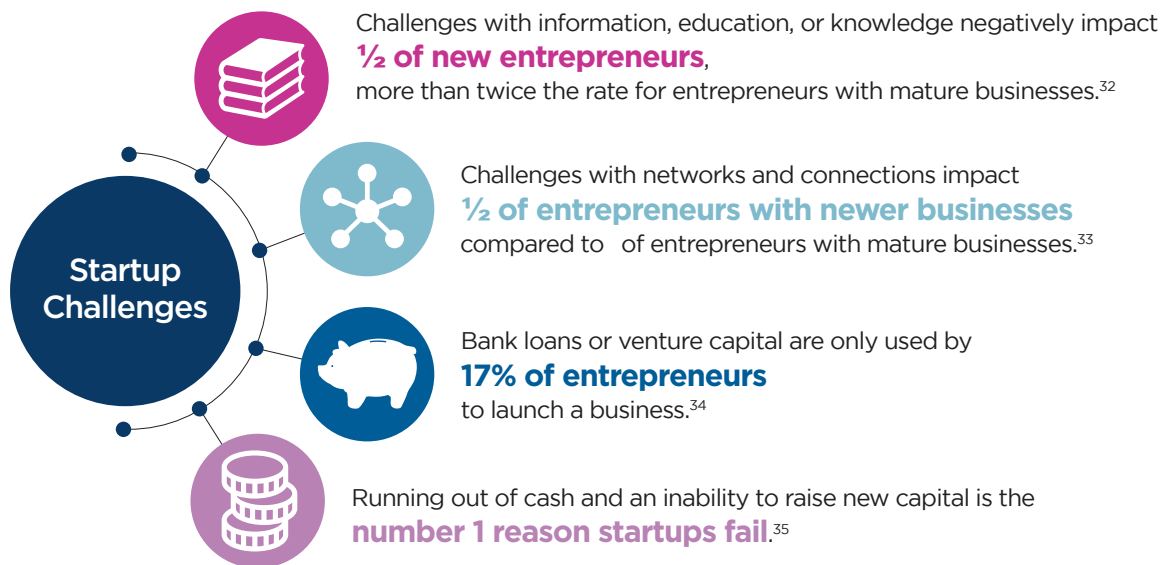


In spite of the decline in overall entrepreneurship numbers, a record-breaking **1 million new “high propensity businesses,”** meaning those likely to hire employees, were formed in the first six months of 2021.³⁰

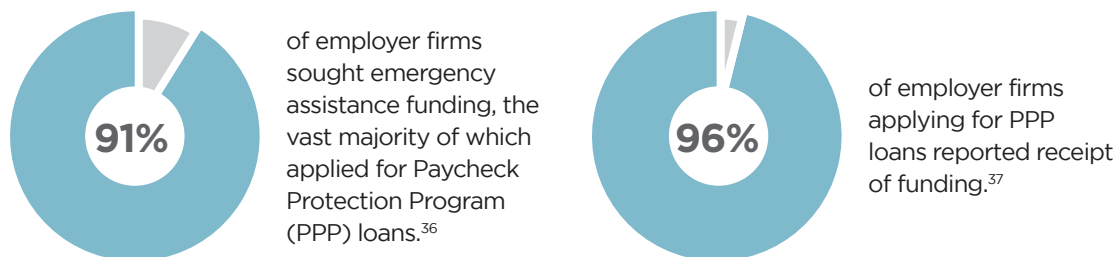
Support for small businesses is critical, as they remain the primary generator of net new jobs in the country from 1995-2020.³¹



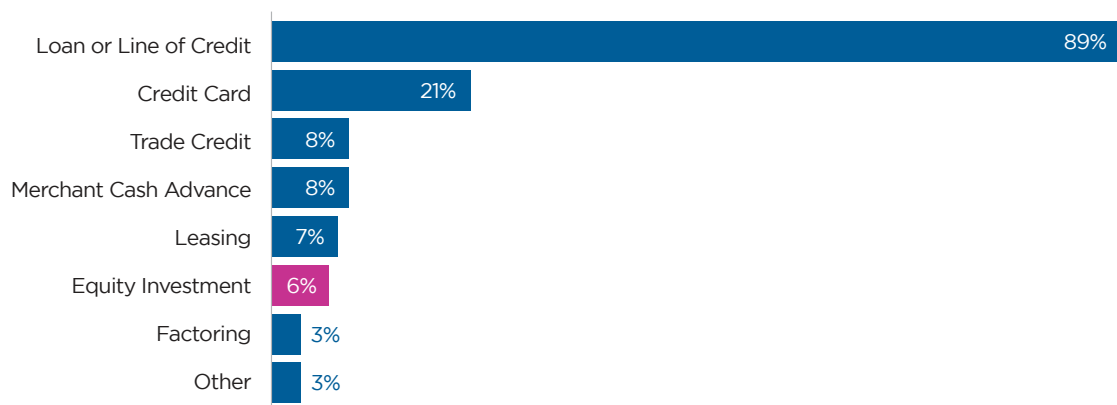
Early-stage entrepreneurs report struggles as they build new companies



COVID-19 emergency assistance played a critical role in funding small businesses.



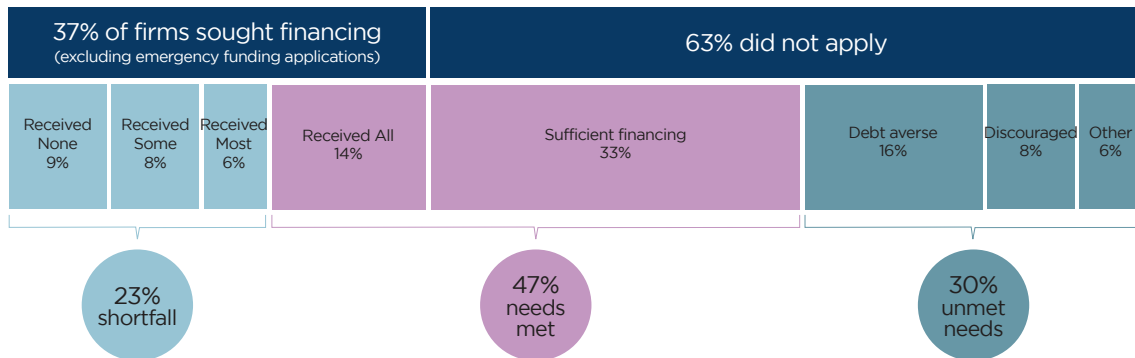
Equity investments remain only a small portion of external capital funding for small businesses³⁸



Small businesses encounter varying degrees of success in meeting their funding needs through debt financing.³⁹

Access to credit from lenders is vital for the survival and growth of many small businesses.⁴⁰

However, emerging businesses typically have minimal or no collateral and lack sufficient earnings histories, tax returns, and performance track records for bank underwriting.⁴¹

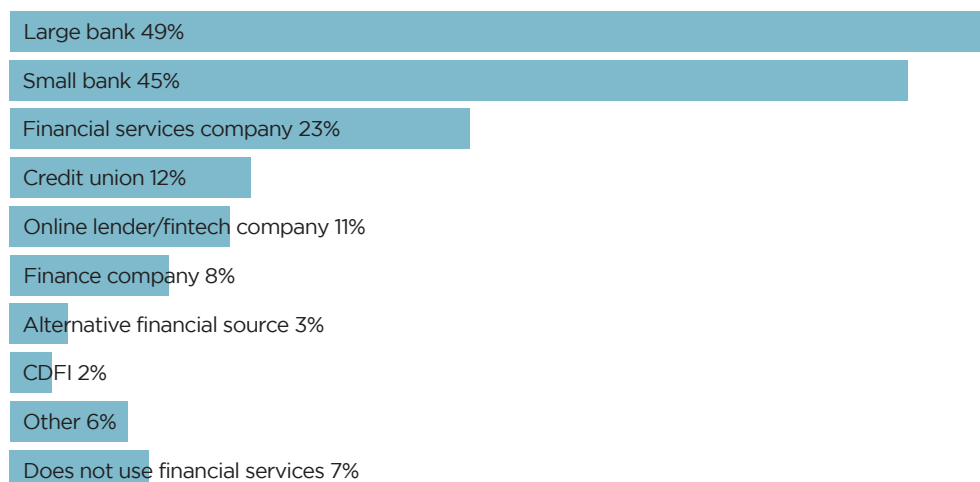


Discouraged borrowers report not applying for a small business loan for a variety of reasons.⁴²



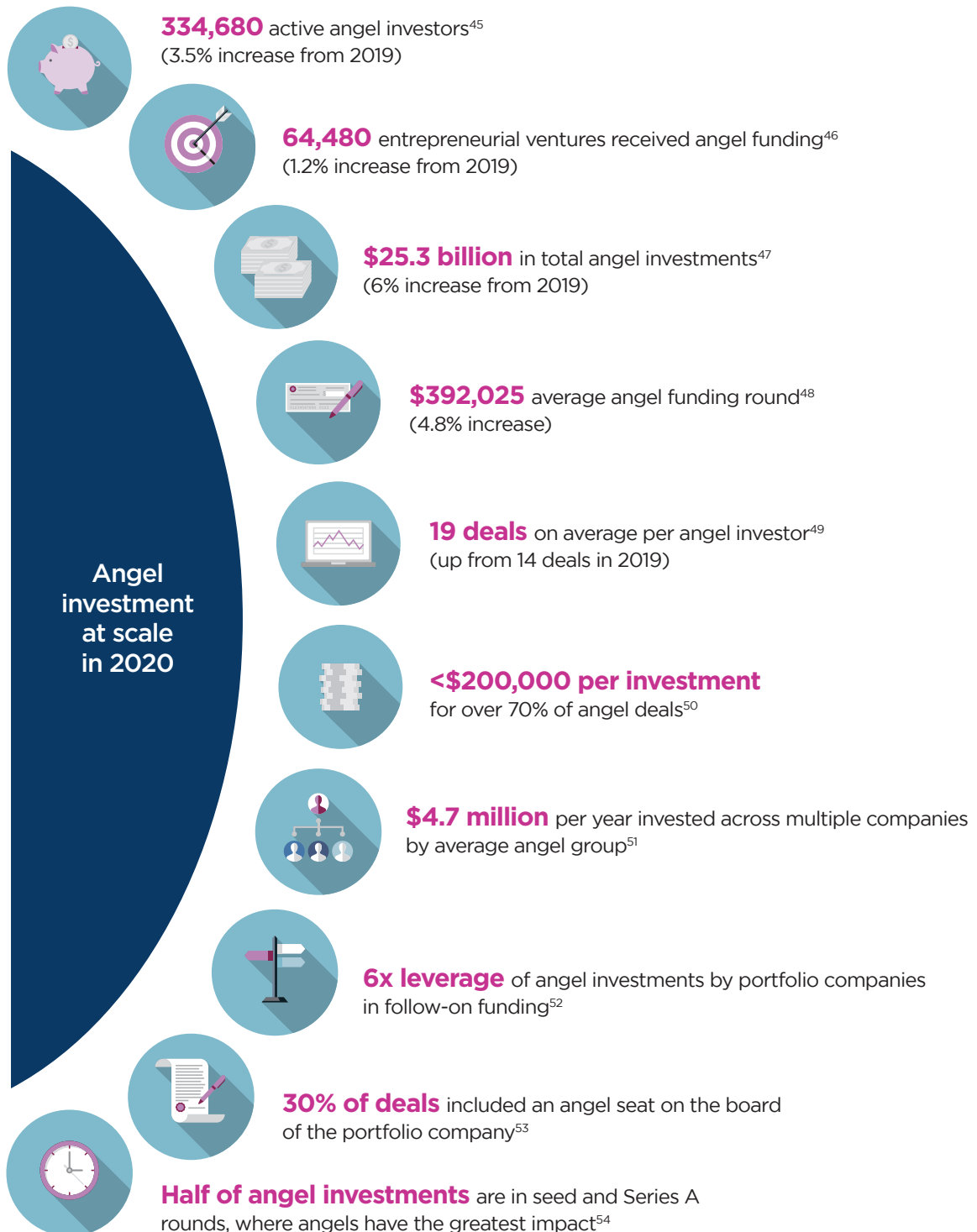
In the absence of business collateral, banks often rely on personal wealth information about the founder or entrepreneur to determine loan default probability.⁴³

Small businesses seek financial services from a wide variety of service providers, with 83% of firms using either a large or small bank.⁴⁴



Angel investors are a significant source of early-stage capital

Angel investors are generally high-net-worth individuals who invest their own money directly in emerging businesses, typically in early funding rounds. Most angel investors are accredited investors, and many are current or former entrepreneurs themselves.



How is seed funding changing?

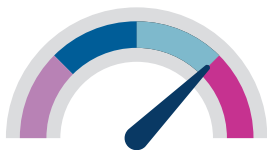
The seed round is typically a company's first funding round, often raised from friends and family, angel investors, or early-stage funds in exchange for a convertible note. Capital at this stage is often used for product development and market research.⁵⁵



Diversification is the primary risk mitigation technique for seed investors. Most seed firms make a lot of smaller bets relative to their fund size — for instance, a modern seed fund might be \$250 million and make 50 to 80 investments, spreading the risk wide.

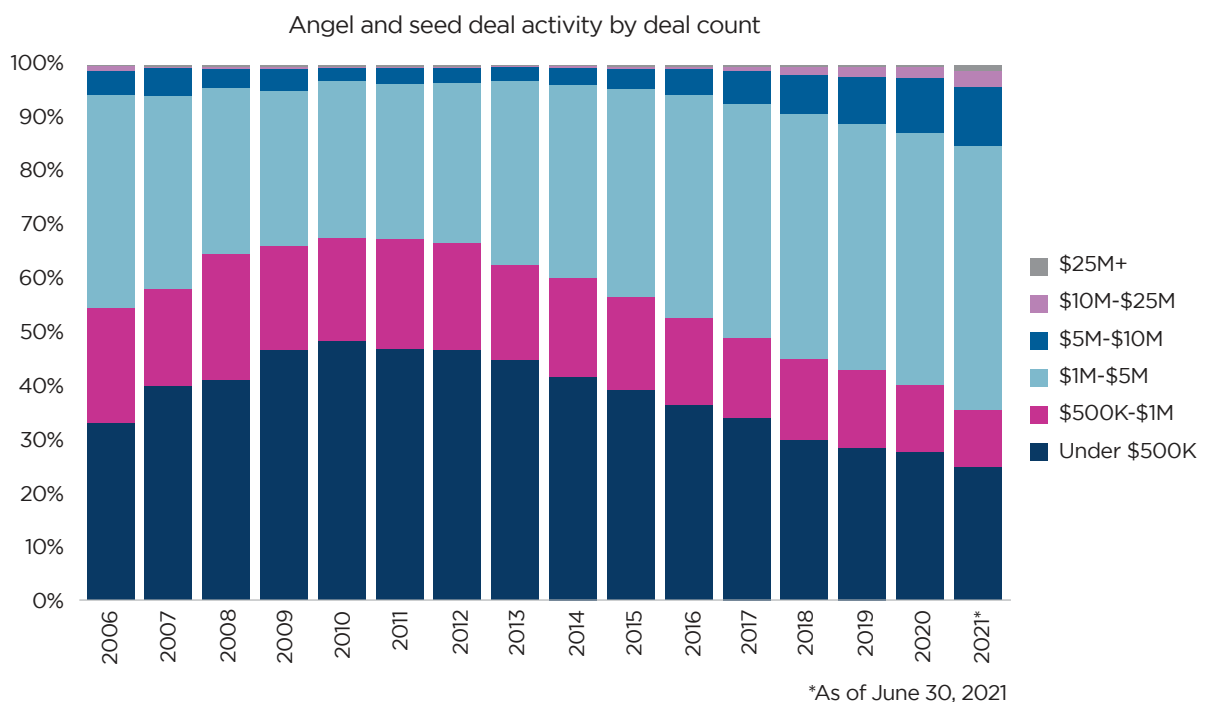
TECHCRUNCH⁵⁶

In recent years, the seed stage has begun attracting large, multi-stage institutional investors eager for earlier deal exposure.⁵⁷



As a result, the first half of 2021 has already surpassed the total angel and seed deal value of every year prior to 2017, with more than **\$7.0 billion in capital invested**.⁵⁸

Angel and seed deal sizes continue to creep higher with earlier investments by institutional and later-stage players.⁵⁹



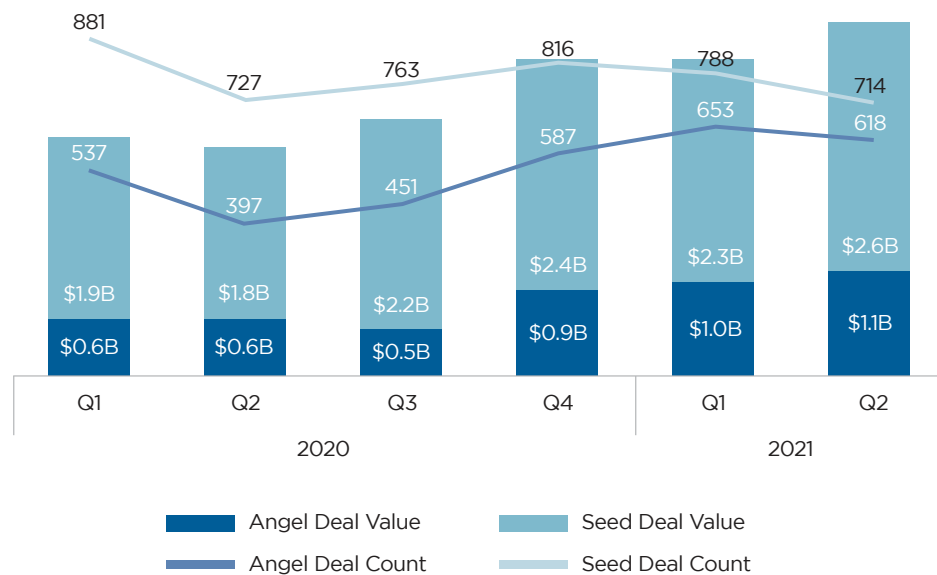
Angel and seed deals have expanded beyond tech hubs, but remain very localized.

The scale of local angel investment activity is closely correlated with the areas with the highest VC activity.⁶⁰ More than one-third of angel and seed deals occurred in areas other than the top 10 funding hubs.⁶¹

Both individual angels and angel groups tend to focus on their local communities.
The distance between lead investors and the target company averages only



By deal count and value, both angel and seed activity have increased in 2021.⁶³

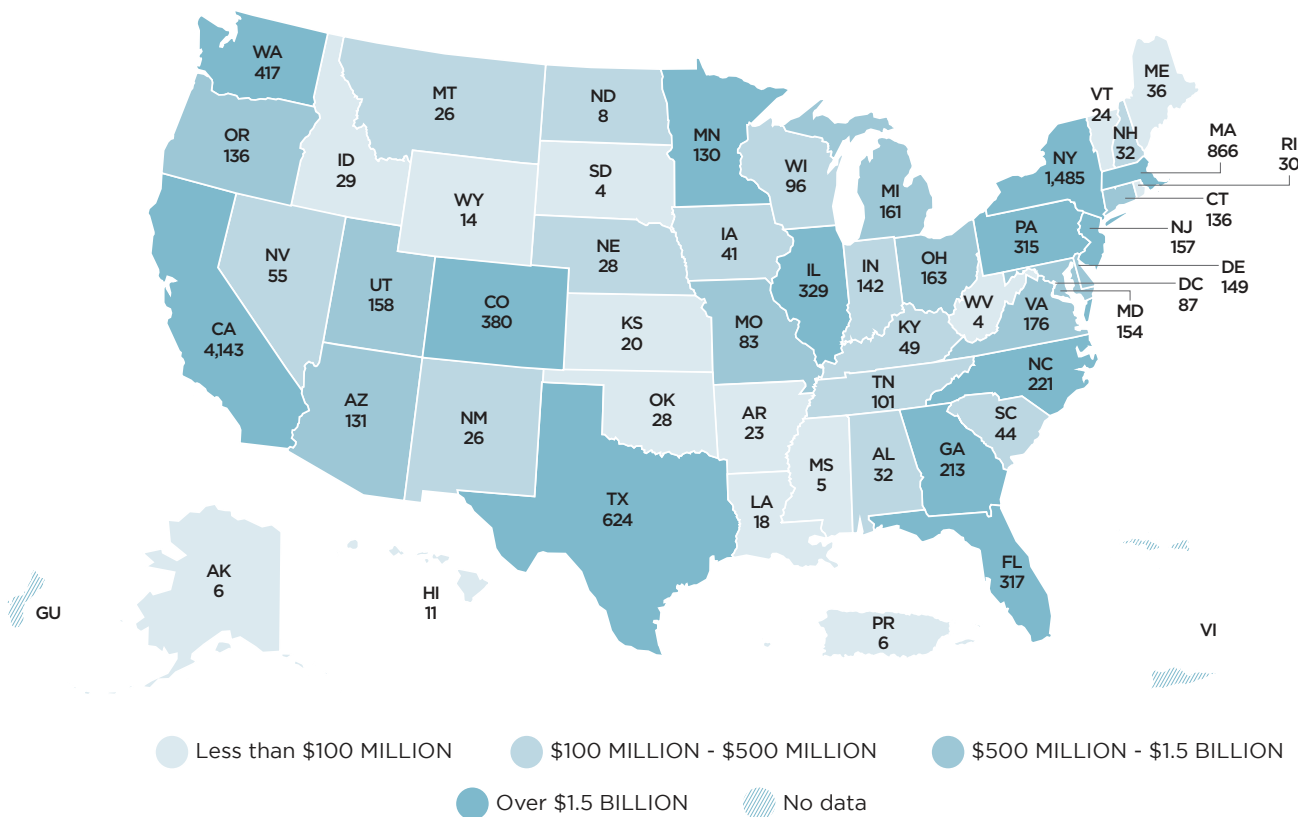


Mature and Later-Stage Businesses

Companies within this segment of the market are generally growing and looking for larger amounts of capital that can fund operations of scale, ventures into new verticals, and preparation for public markets. Most often their investors are institutional in nature, whether VC funds, private equity funds, or increasingly crossover investors from the public market.

Although concentrated in tech hubs, growth startups backed by VC exist across the country

The below map illustrates the concentration of estimated VC deal value in 2020, with the number of VC deals indicated on each state.⁶⁴



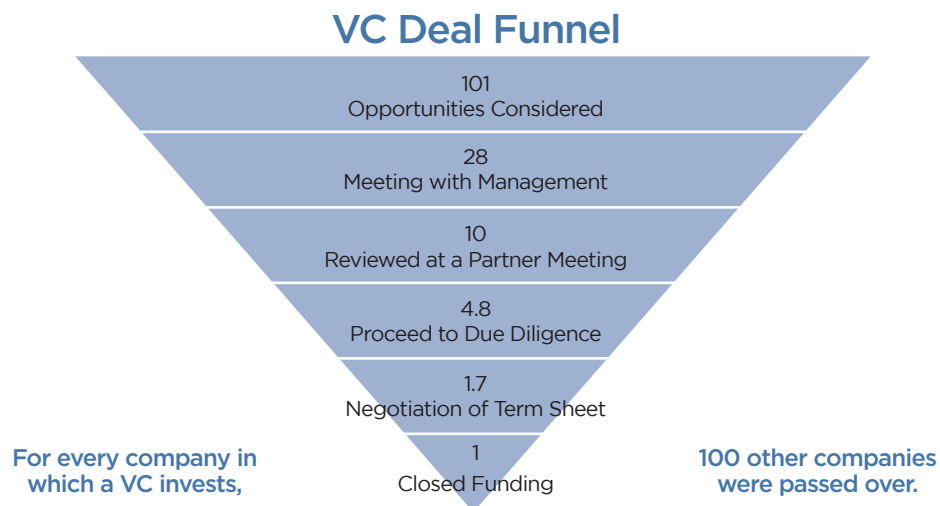
How are mature and growth companies interacting with VC investors?

Network connections are still the dominant source of VC deal flow.

VCs are more likely to connect with new startups by relying on their existing networks for leads and introductions, leaving few opportunities for entrepreneurs without personal or professional network connections.⁶⁵



For entrepreneurs who do pitch to VC investors, the odds of securing funding are exceedingly low⁶⁶

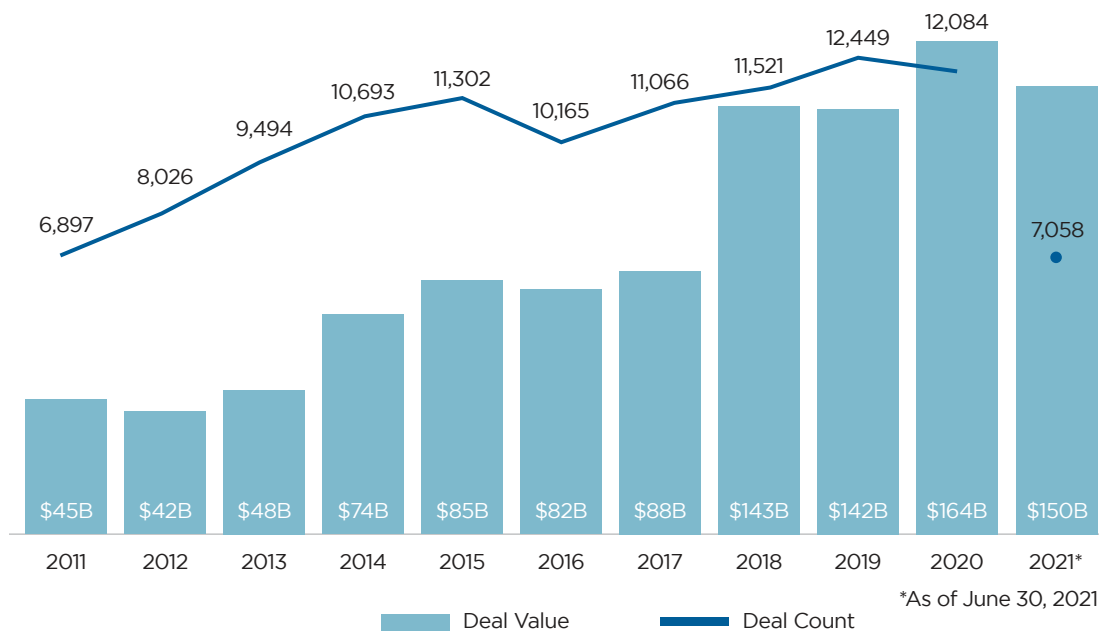


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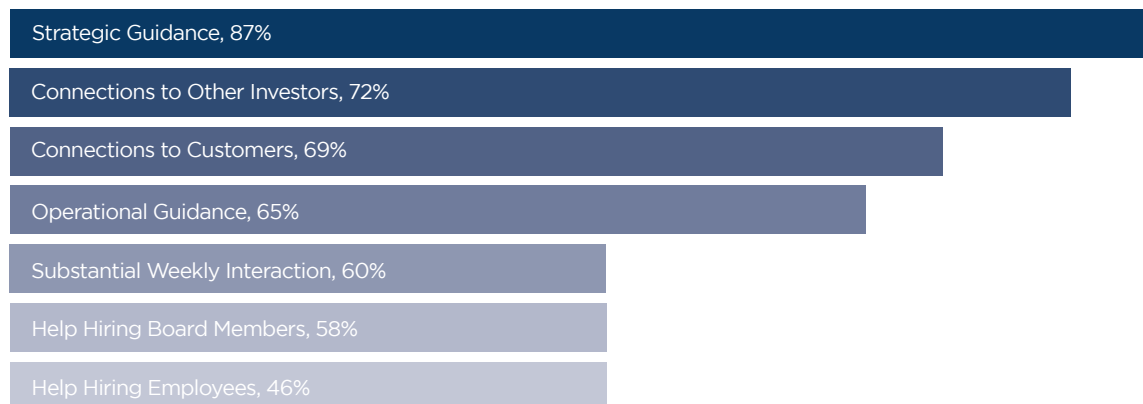
As we look forward over the next decade, the reality is we can't just continue to invest in the communities and ecosystems that have driven a lot of the economic upside that we have seen over the last 20 years that tech has been driving. We are going to have to seed and start to invest in communities in flyover states, tier two markets that will become tier one, and in different communities themselves. An emerging manager is a key part of that because networks ultimately are a fundamental part of this ecosystem.

FREDERIK GROCE⁶⁷

VC deal value has surged in recent years and is on track for a record-breaking 2021.⁶⁸



Traditional VC investors are active advisers to their portfolio companies, providing an array of services.⁶⁹



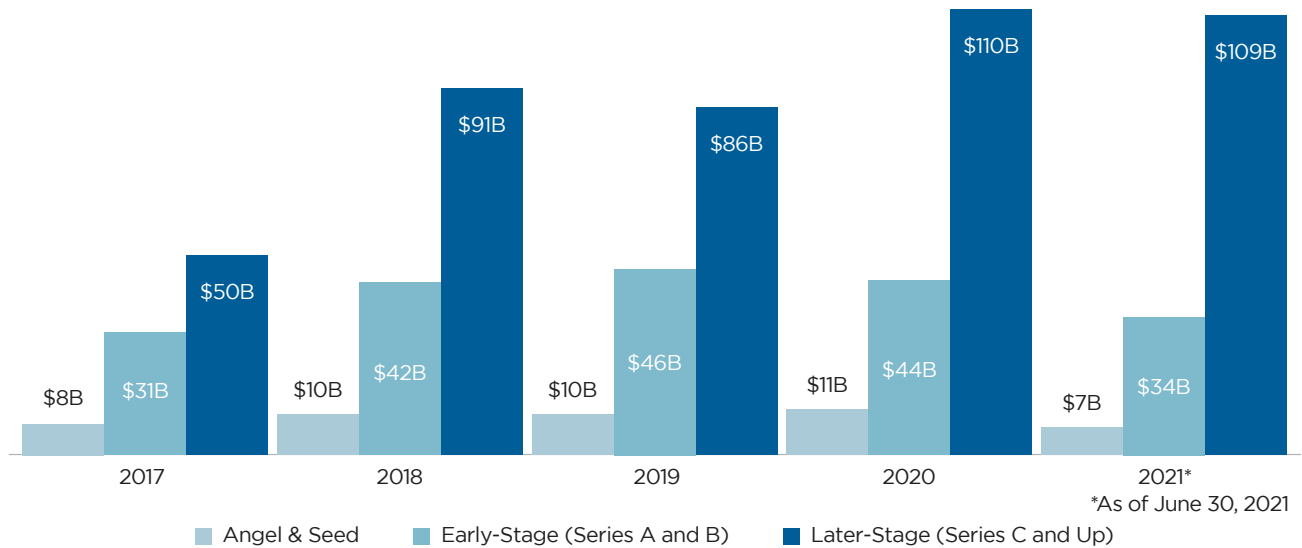
Raising a Series B seems to be the most uncertain point in a typical startup journey. Not only do Series B rounds take 100 days longer to close on average than Series A rounds do, they have the highest variance of any raising event.

CARTA⁷⁰

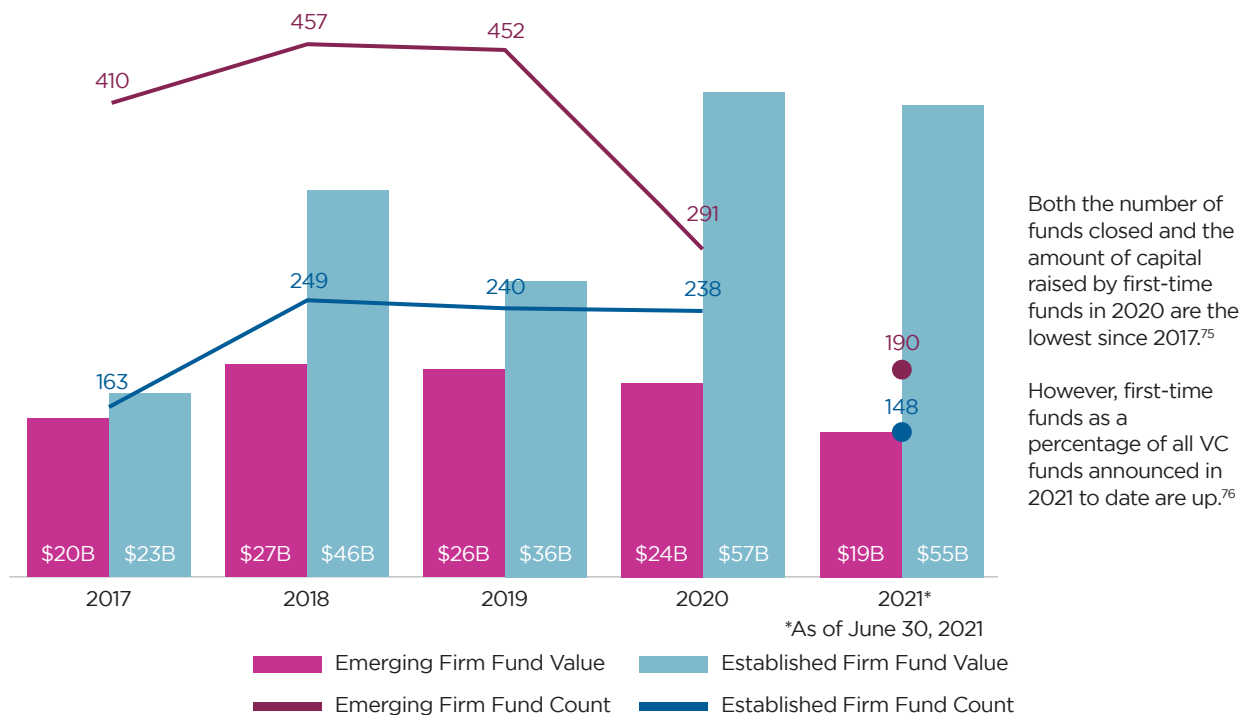
How is VC investment activity changing?

Last year the pandemic forced many firms to focus their attention on later-stage businesses at the expense of angel/seed and early-stage businesses.⁷¹ However, early-stage deals have rebounded to new heights, with a median Series A round raising \$10 million in Q2 2021.⁷²

2021 is on track to break records across each stage of VC investment.⁷³



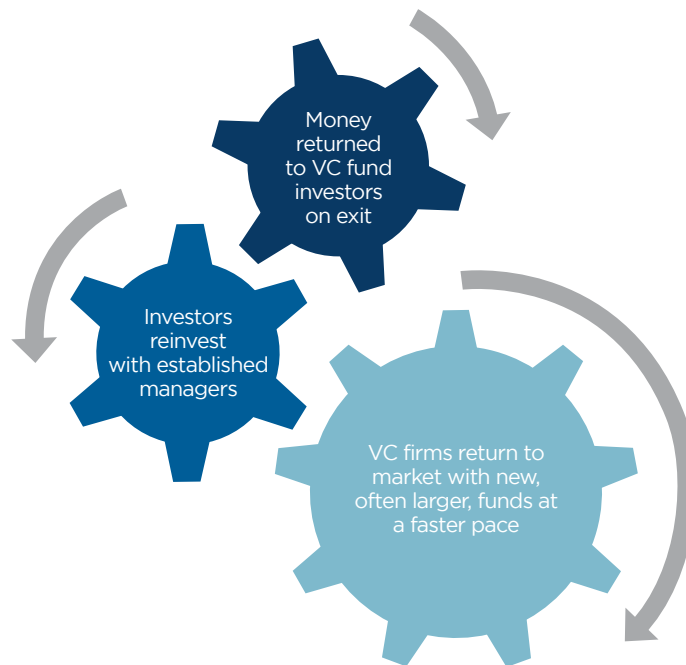
Fundraising by new and emerging managers has not kept pace with record levels of overall venture fundraising.⁷⁴



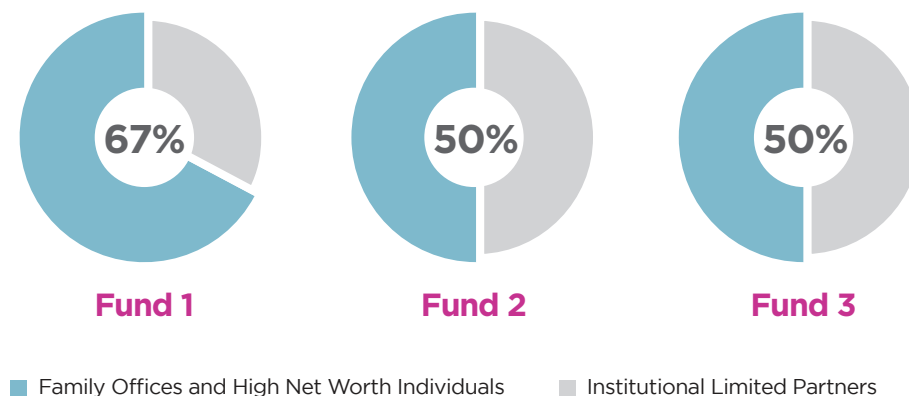
What trends are shaping the investment activities of limited partners (LP) in VC funds?

Recent portfolio company exits have fueled reinvestments by LPs into new VC vehicles.

Liquidity events reached record heights in 2020, with total exit value of \$287.5 billion.⁷⁷

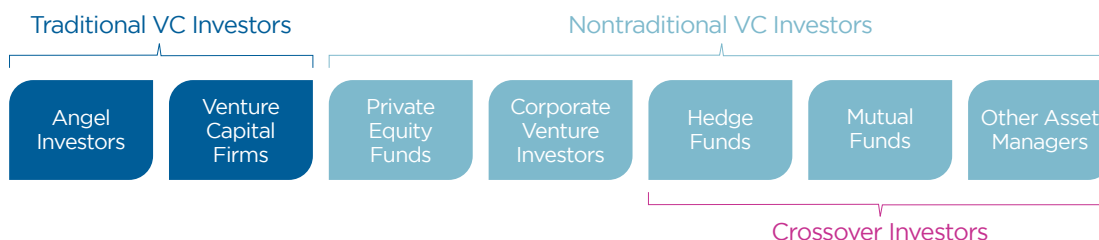


Family offices and high net worth individuals are the dominant backers of new and emerging fund managers, especially on Fund 1.⁷⁸



What is the impact of nontraditional investors on mature and later-stage fundraising?

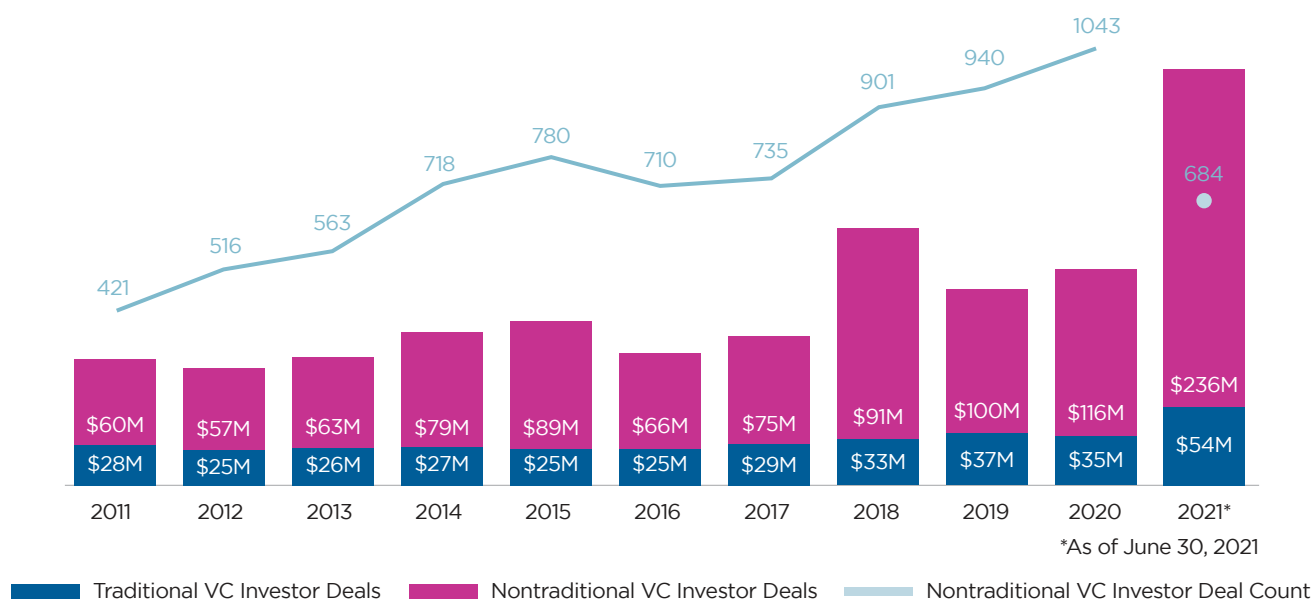
Over the last few years, nontraditional investors—generally firms and institutions not labeled as VCs—have increasingly crossed over from the public markets to also invest in mature and later-stage financing rounds, often with dramatic impacts on company valuation and deal size.⁷⁹



Crossover investors are typically buy-side public equity asset managers that also invest in privately backed companies. By incorporating private companies into their investment strategy, crossover investors can invest earlier in the company life cycle, thereby acquiring larger equity stakes in promising startups with the hope of seeking venture-level returns.

PITCHBOOK⁸⁰

Nontraditional investor participation is driving up median pre-money valuations in later-stage VC deals.⁸¹



Crossover investors bring other strategic value to companies besides capital, preparing them for entry into the public market.⁸²



strategic valuation

giving credibility to the cap table from public market investors



streamlined IPO

with access to board members, advisors, and public market expertise



credibility

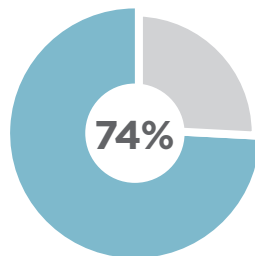
before companies begin testing the IPO waters



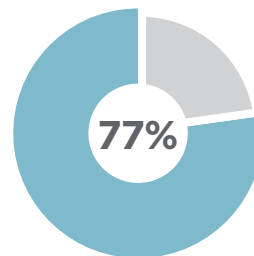
diligence signals

for potential IPO investors

A significant percentage of companies going public in 2020 were backed by crossover investors.⁸³

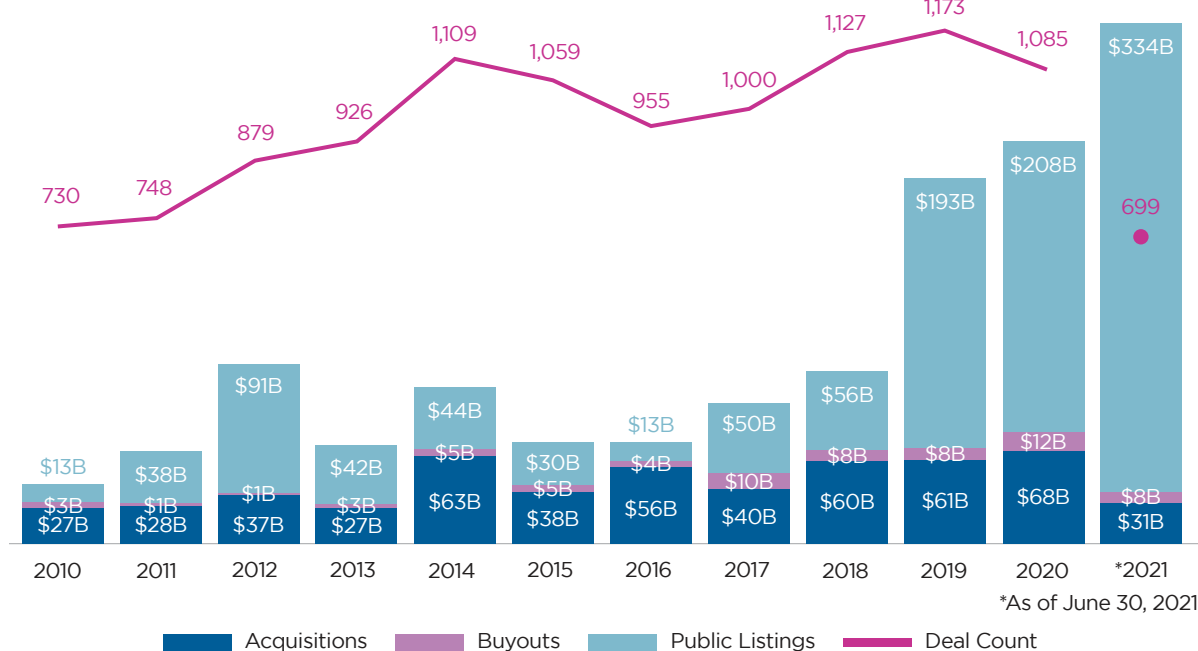


IPOs by Count



IPOs by Value

Venture-backed exit activity in the first half of 2021 has already surpassed the 2020 high water mark by nearly 30%, fueled predominantly by public listings.⁸⁴

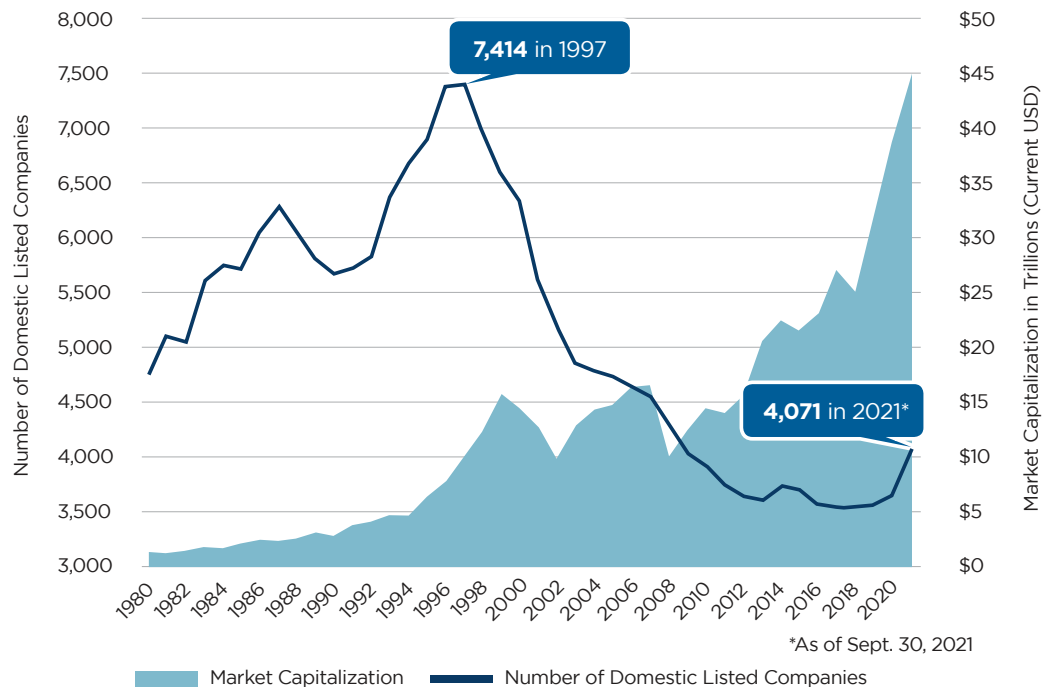


Small Public Companies

Companies can access broad pools of investors when they conduct public offerings, allowing companies to raise large amounts of capital to fund activities, such as research and development, capital expenditures, or debt service. Public offerings also provide liquidity to early-stage investors and publicity for the company's products and services.

How has the prevalence of U.S. publicly-traded companies changed over time?⁸⁵

The number of publicly-traded companies has declined since its 1997 peak preceding the dot-com bubble. Recently, the rate of increase in publicly-traded companies has gone up significantly due to the thriving IPO market.



However, looking at number of listed companies in isolation misses the bigger picture on public market trends.



Even after adjusting for inflation, the **market capitalization** of public companies has continued to soar to new heights.



When taking into consideration the mergers of private companies into public companies rather than those companies going public directly, the listing gap is actually much smaller.⁸⁶

What are the different pathways to going public?

Besides the record-breaking number of deals and amounts raised in traditional IPOs over the last year, companies have also been using different routes, such as direct listings and SPACs, to go public. While these alternative pathways have become popular in recent years, many factors play into which pathway a company chooses.

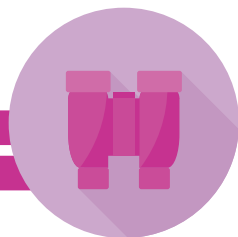


Traditional Initial
Public Offering (IPO)

What is it? A private company raises capital by selling newly-issued shares to investment banks (underwriters), which they then sell primarily to institutional investors.

Why choose this path? An IPO is the traditional way for companies to go public. Companies may choose this path to have more control over their initial investor base and obtain an underwriter's assistance in marketing and managing initial trading volume.

What to consider? The transaction costs, including underwriter fees, are high, and the process typically takes a long time.



Special Purpose
Acquisition Company
(SPAC)

What is it? A SPAC goes public as a shell company using an IPO. Generally within two years, a SPAC combines with a private company (target) via a de-SPAC merger, with the resulting company becoming public and receiving a combination of the SPAC's IPO proceeds and additional capital from a private financing.

Why choose this path? By going public via SPAC, companies can have certainty as to the amount raised, potentially a shorter timeframe than the traditional IPO process, and a strategic partnership with an experienced management team that sponsors put together.

What to consider? The overall transaction costs for target companies can be high, and they must also consider equity dilution from sponsors and other private financing investors, which is why SPACs tend to draw bigger companies looking to go public.⁸⁷



Direct Listing

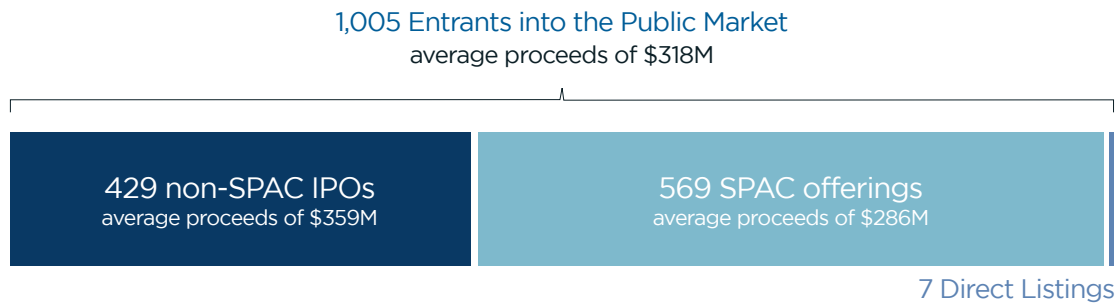
What is it? A private company becomes public, typically without raising new funds in the process, by allowing existing shareholders to sell shares directly to the public.

Why choose this path? Historically, a few large, consumer-facing companies have chosen this path due to potentially lower transaction costs and other business-specific reasons.

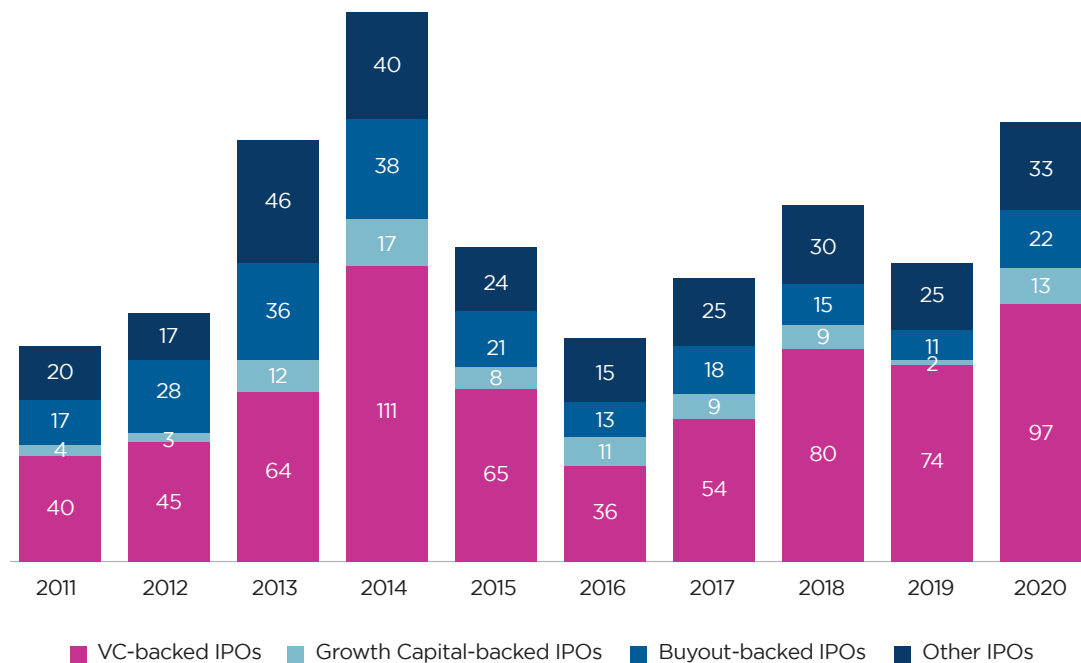
What to consider? With no underwriters involved, companies will have no control over their initial investor base and may face trading volume challenges, which is why companies that choose this path are often ones that have strong brand recognition that can generate sufficient market interest.

How are the dynamics changing for companies going public?

The past year has marked one of the busiest years for the public market. From July 1, 2020 through June 30, 2021, there were:⁸⁸

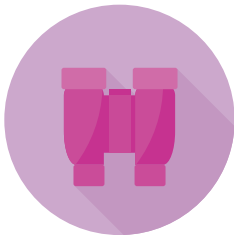


The number of IPOs has varied over the last decade; however, VC-backed companies continue to be the majority of exchange-listed IPOs.⁸⁹



Investors are increasingly focused on environmental, social, and governance (ESG) considerations for public companies.

ESG considerations are becoming more important for many public companies, with investors increasingly focused on them and expecting newly-public companies to communicate how ESG is incorporated into their business plans and operations.⁹⁰



ESG SPACs

In 2020, more than 20 SPACs with an ESG focus have launched, raising more than \$5 billion in the aggregate.⁹¹



Investor Demand

Millennials are driving change, with 95% interested in sustainable investing and 41% already invested in companies that have goals of producing positive ESG outcomes, compared to 28% of individuals in general.⁹²

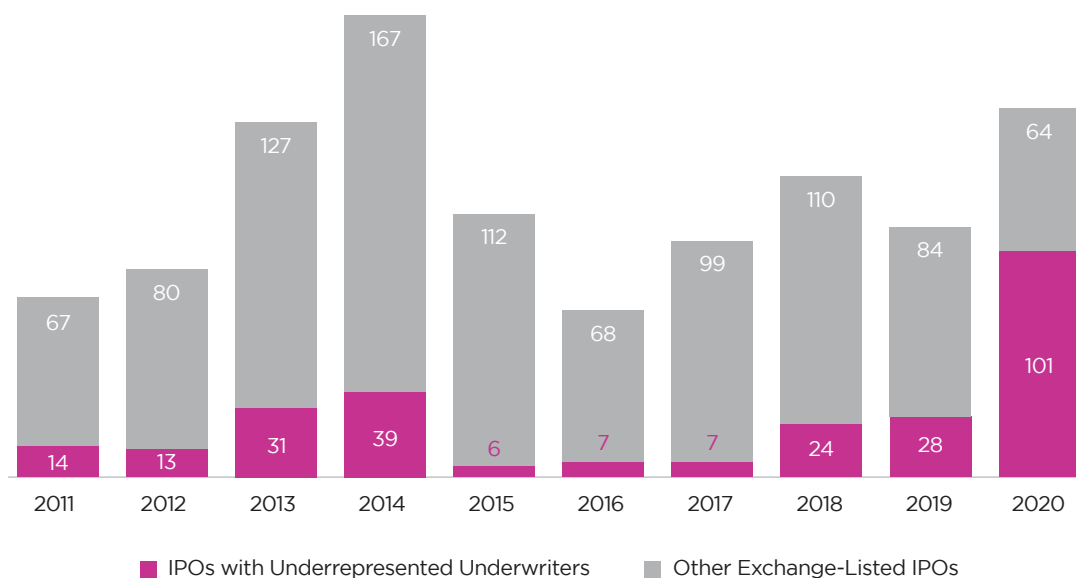


ESG-Aligned Capital

Having strong ESG credentials can help attract ESG-aligned capital from private and public investors focused on sustainability, while also increasing access and valuation in debt capital markets.⁹³

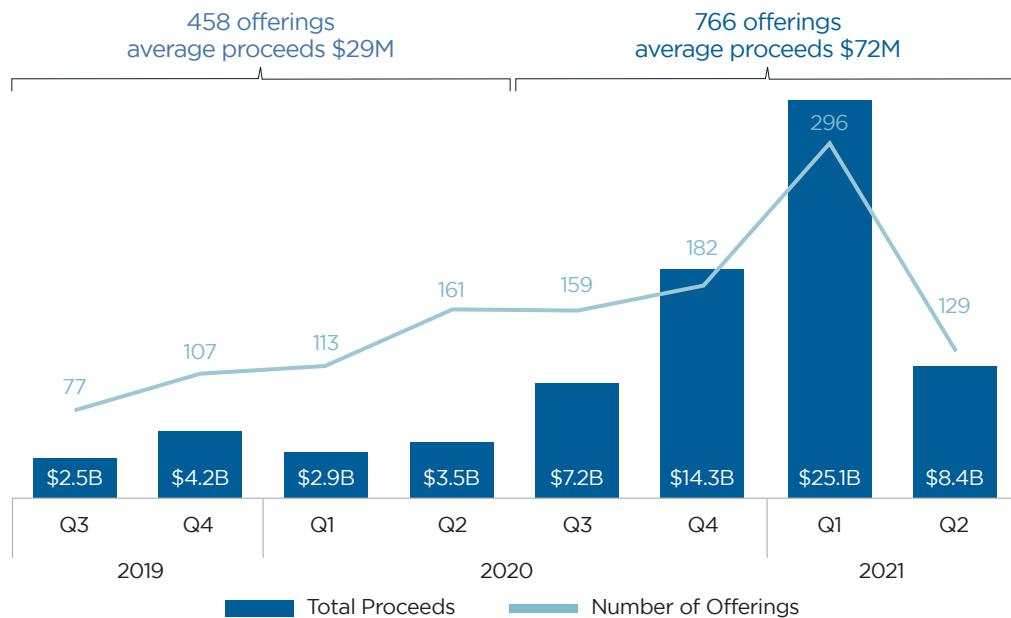
Stakeholders—including investors, exchanges, and customers—are driving public companies to focus on diversity and inclusion both internally and externally.

In recent years, companies have been seeking to support diversity and inclusion by increasingly hiring IPO underwriters classified as minority-, women-, or veteran-owned firms.⁹⁴

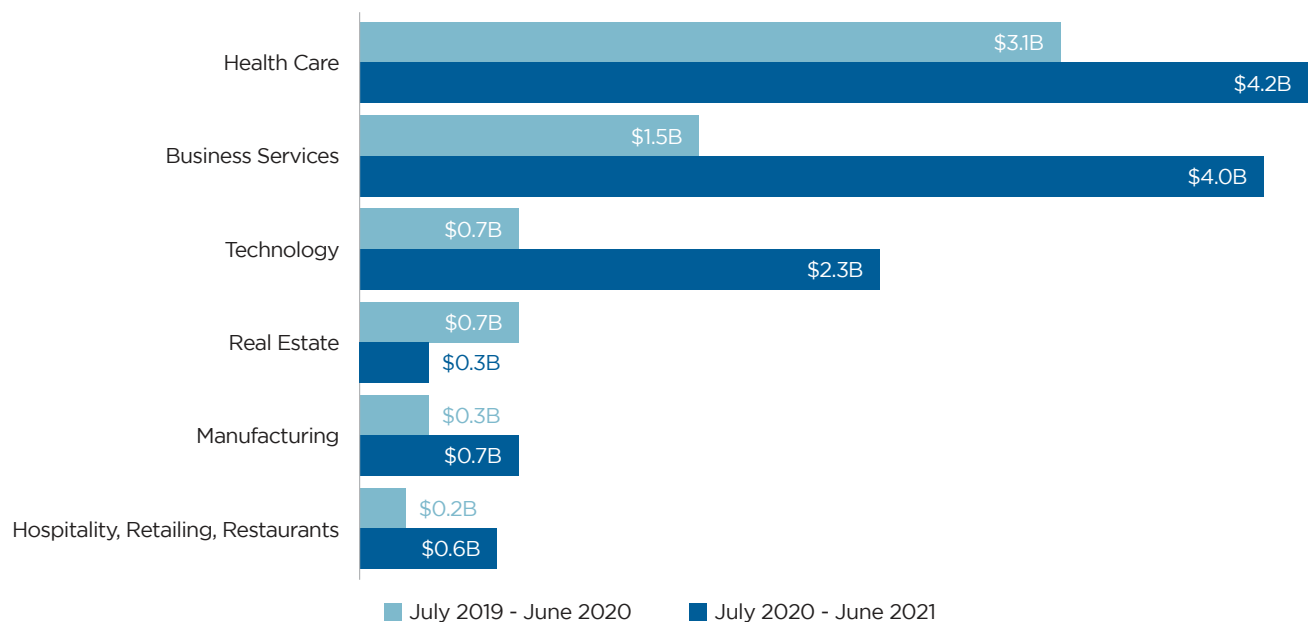


How do small public company trends compare to the public markets at large?

While the press often covers deals by large public companies or “unicorn” private companies, small public companies have also seen growth in equity offering activity over the last year.⁹⁵

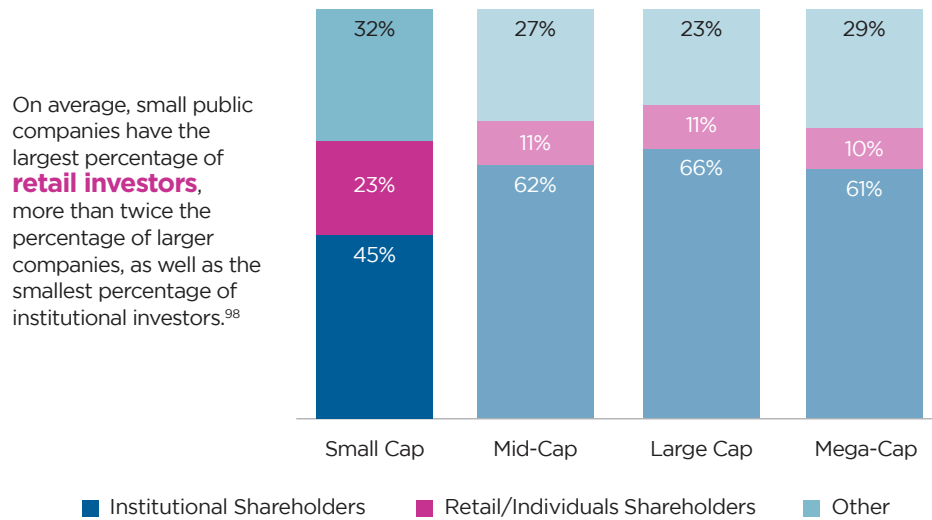


While industry trends remain relatively consistent with the prior year, business services and technology saw the most dramatic increases among equity offerings by small public companies.⁹⁶

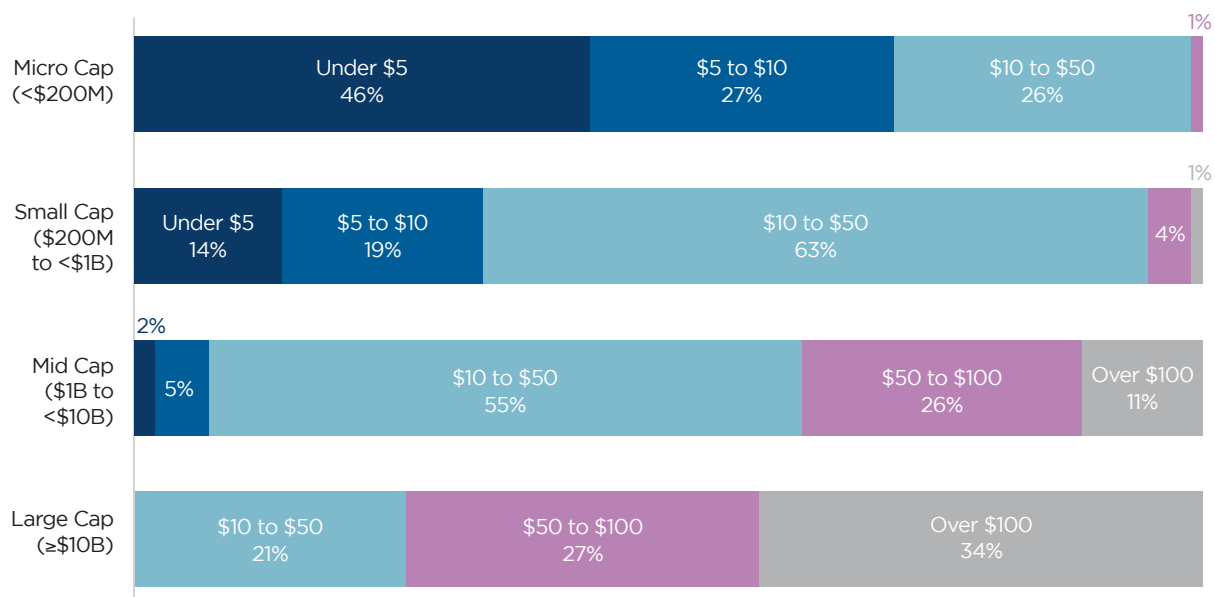


Small public companies are seeing an increasing number of retail investors in their shareholder base.

Nearly 30% of public companies have seen an increase in retail investment in the past 12 months, while more than 25% of companies have seen an increase from three years ago.⁹⁷

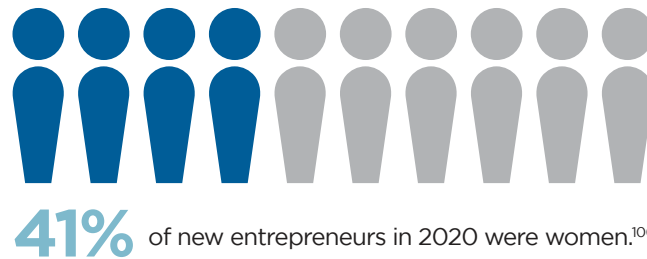


Stock prices vary significantly by market capitalization, with smaller companies tending to have smaller prices.⁹⁹



Women Business Owners and Investors

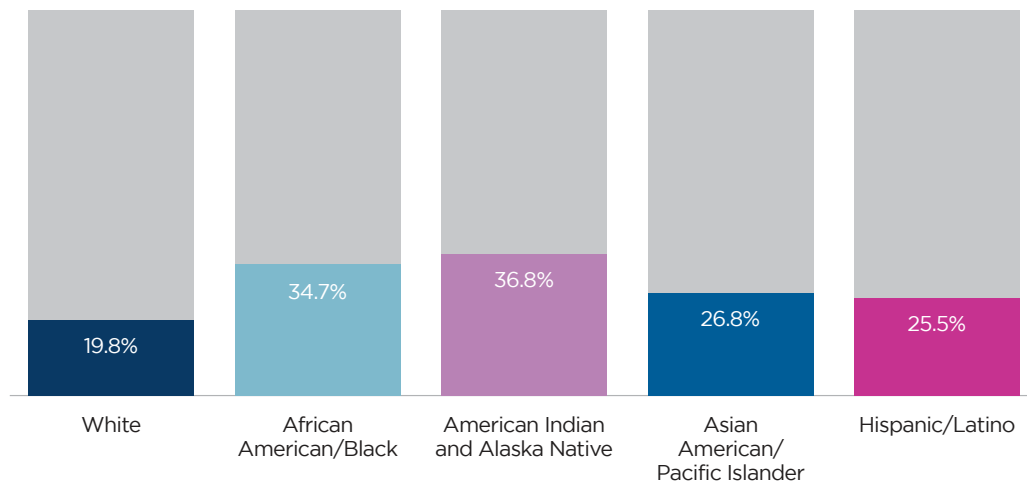
Trends in Women-Owned Business Formation and Ownership



Women own
1.1 million employer firms
across the country.¹⁰¹

Women-owned firms
employed 10.1 million workers
across the country.¹⁰²

By share of employer firms, women owners are underrepresented in every demographic group.¹⁰³

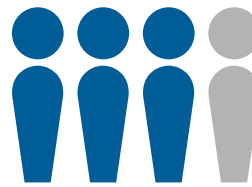


Women entrepreneurs often wear multiple hats, bearing significant household responsibilities outside of running their businesses.¹⁰⁴



1 in 4

reported being the sole provider in their household.



3 in 4

reported their income contributes to at least half of their household finances.

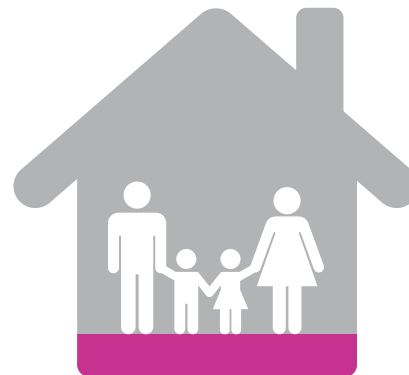
The COVID-19 pandemic has disproportionately impacted women-founders, particularly those with family care responsibilities.¹⁰⁵

The pandemic decimated many service sector businesses, where women tend to own more businesses.¹⁰⁶ On top of steep job losses overall, women founders share unequal family care responsibilities.¹⁰⁷ A recent survey of founder-caregivers found dramatic differences in the child and family-care burden carried by women vs. men founders.¹⁰⁸



11% of women founders reported 7+ hours daily of family care responsibilities pre-COVID.

During the pandemic that burden increased to **56%** of women founders.



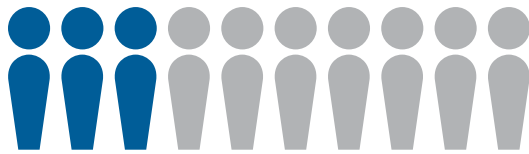
0% of men founders reported 7+ hours daily of family care responsibilities pre-COVID.

During the pandemic that burden increased to **11%** of men founders.

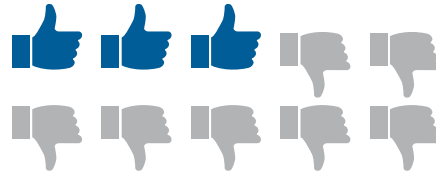
Despite taking on these additional hours of caregiving, women-owned businesses report no greater negative impact to their revenue vs. men founders.¹⁰⁹

Capital Raising Trends for Women-Owned Businesses

Although underrepresentation by gender persists, the investment yield rate among those who do seek angel funding has trended up.

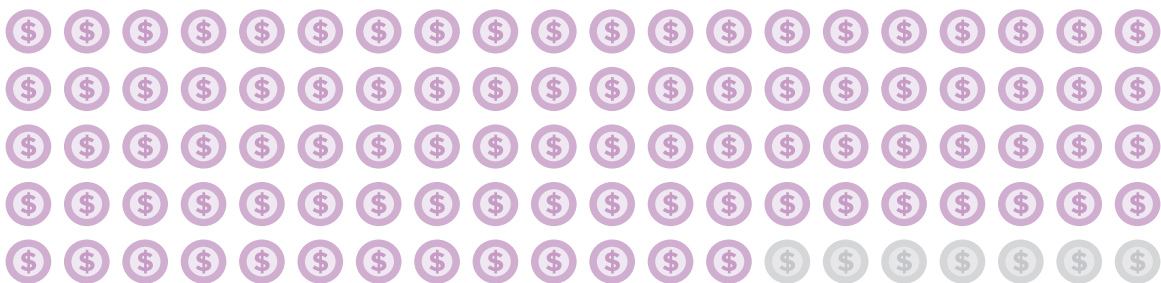


Women constituted
33.6%
of entrepreneurs seeking angel capital
in 2020 (up from 27.6% in 2019),



and had an investment yield rate of
28.1%
(up from 21.4% in 2019), compared
to a baseline rate of 30.8%.¹¹⁰

For every dollar raised by men-CEOs in 2020,



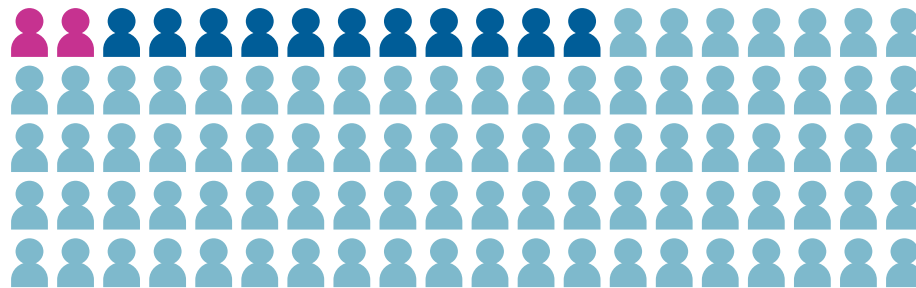
women-CEOs raised **93 cents**.¹¹¹

“

There are many reasons why female founders routinely receive less venture capital than their male counterparts, ranging from sexism and structural bias to the pandemic causing cautious investors to revert to existing white and male networks. One clear catalyst for change, though, is having more diverse decision-makers on boards and cap tables. By stopping money from being handled by the same people, the next generation of investors will be able to break some of the gender gap in fundraising.

TECHCRUNCH¹¹²

While VC investments have soared to record heights in 2020 and 2021, women-founded companies have raised less money relative to men, and attracted a smaller share of total VC investment.¹¹³



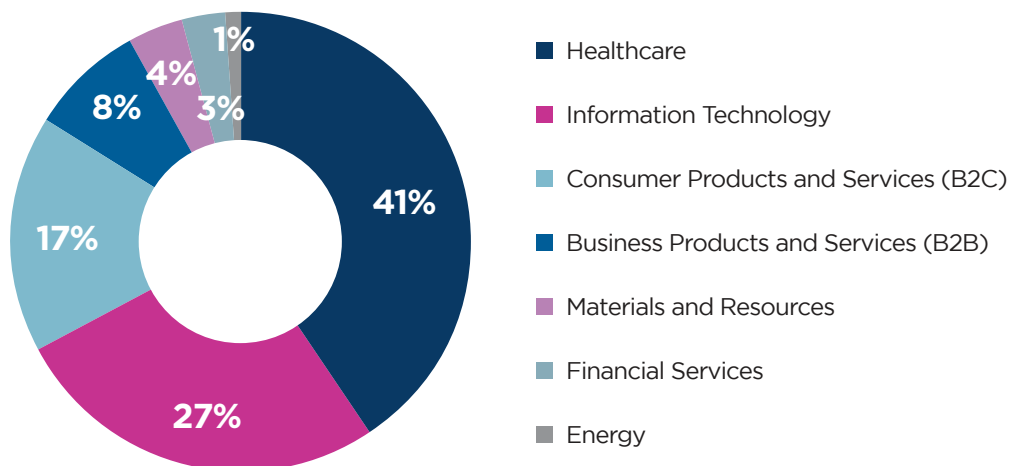
2.3%

of venture dollars went to women-only founding teams in 2020 (down from 3.3% in 2019), and **10.8%** went to women/men co-founding teams (down from 11.9% in 2019).¹¹⁴

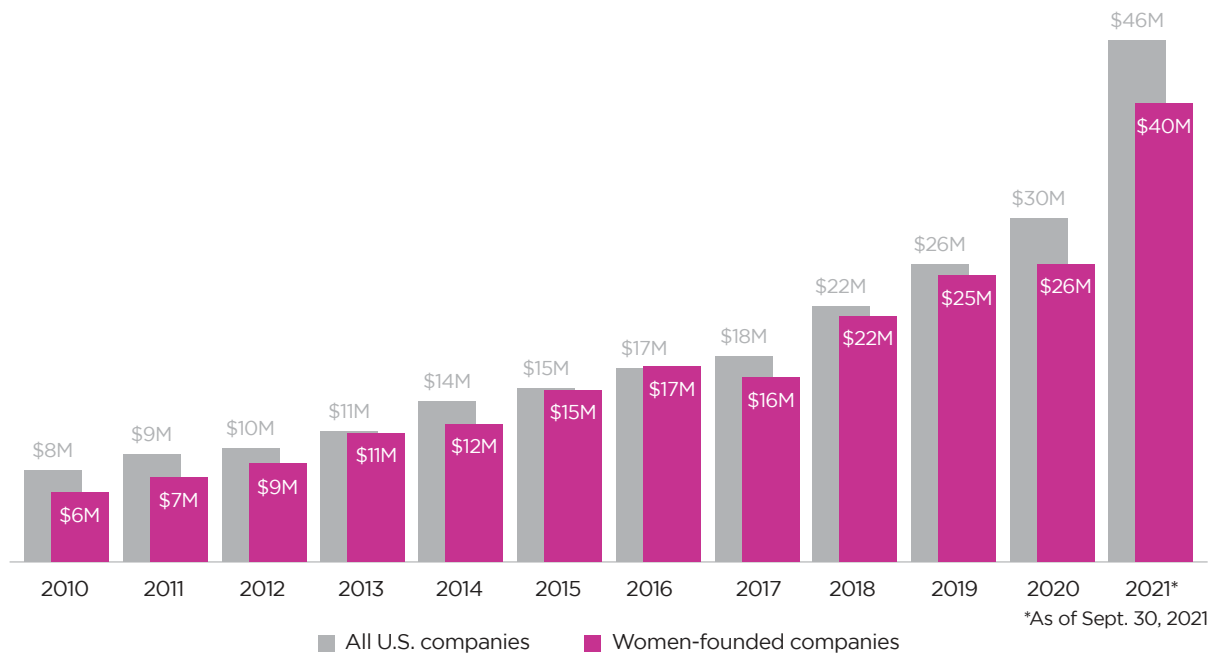


In the first half of 2021, women founders and co-founders raised **\$25.12 billion in venture funding**, more than the total amount raised in any prior year, reflecting the blistering rate of capital raising more broadly in 2021.¹¹⁵

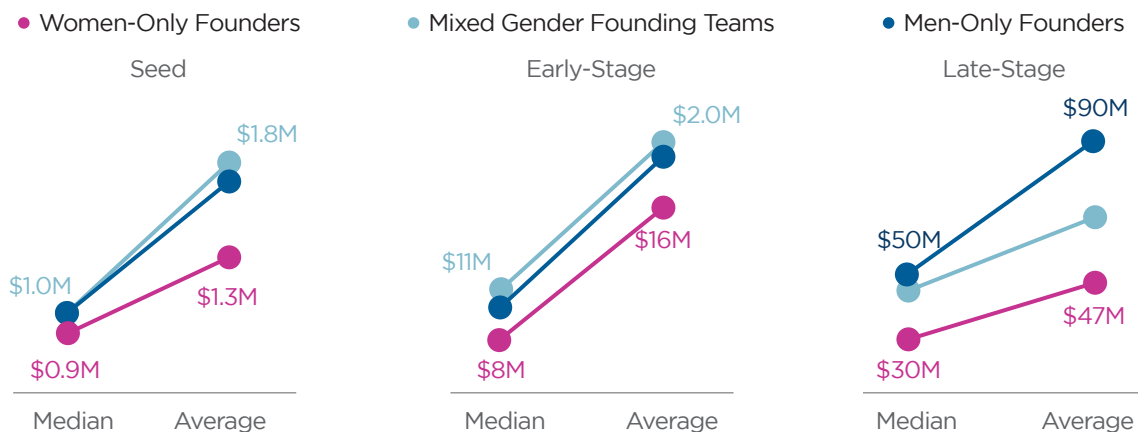
Women-led companies raised venture funding across a variety of sectors in 2020, concentrated most heavily in healthcare and information technology.¹¹⁶



In recent years, women founders have faced a widening gap in early-stage, pre-money, VC valuations compared to all U.S. companies.¹¹⁷



Among the women in 2020 who did raise capital, the women-only founders raised less per funding round than their men counterparts.¹¹⁸



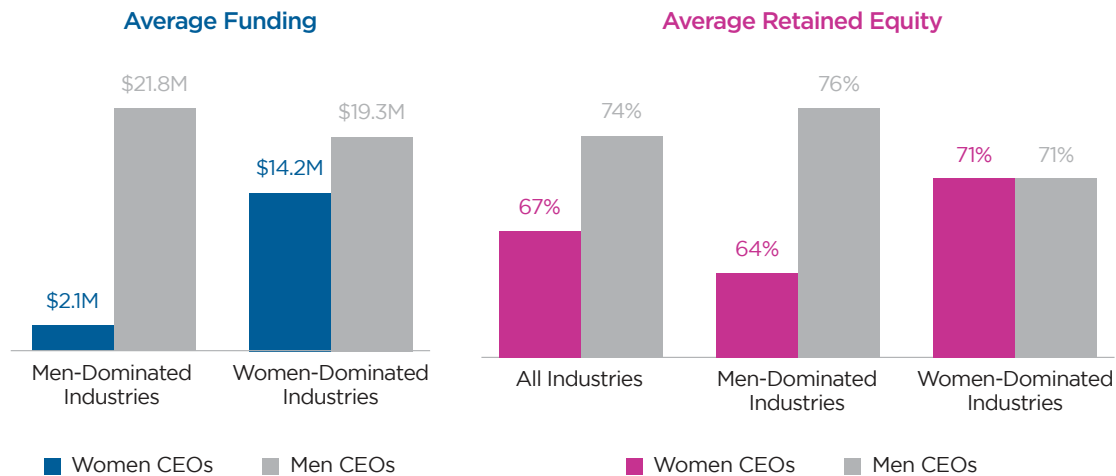
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The financing of the later stage, late-stage venture capital, and private equity is almost no different from the early stages where women are still faced with conversations being very different from the ones men have to deal with.

LAKSHMI BALACHANDRA¹¹⁹

Investors penalize women-founders for perceived “lack of industry fit.”

When women-founders raise capital in industries dominated by men, they both raise less capital and retain less equity than their men counterparts, evidence of investor bias continuing to hold women back in obtaining funding.¹²⁰



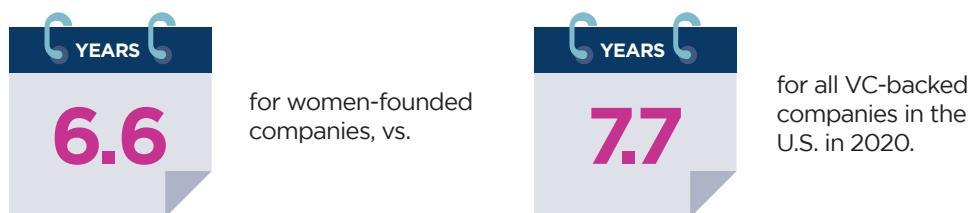
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The benefit of a gender diversity helps mixed-gender teams raise funding, but only when they are led by a male CEO. The consistently lower funding allocation, both in total and on average, to mixed-gender teams when they are led by women CEOs points to the severity of gender bias in startup capital allocation.

CHRISTOPHER CASSION, ET AL.¹²¹

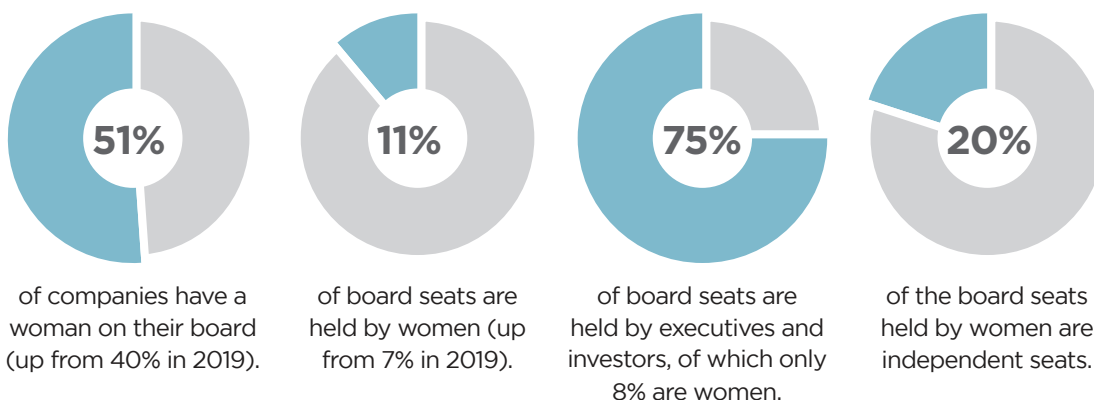
Despite challenges in securing funding, women-owned businesses continue to outperform the overall VC market.

Women-founded companies are exiting and returning capital to investors one year faster on average than men-founded companies:¹²²



Women in Leadership Roles

While women remain underrepresented in board roles among venture-backed private companies, the numbers improved in 2020.¹²³



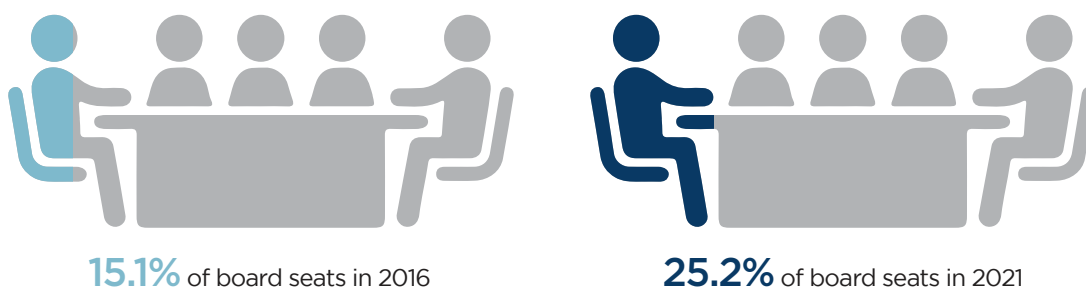
The leadership of private companies ripples into the public markets.

Historically, thousands of CEOs have founded and led companies through an IPO to be exchange-listed; however, only about 20 of those were founded and led by women.¹²⁴

Of the 442 companies to go public by mid-December 2020, **only four were founded and led by women.**¹²⁵

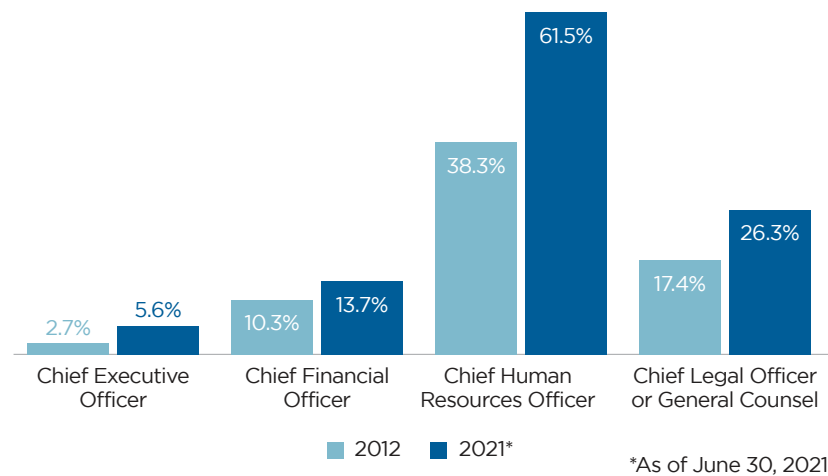


Women's share of board seats of Russell 3000 companies has seen some improvement in recent years.¹²⁶



However, only **2.9%** of the Russell 3000 (84 companies) boards of directors have achieved gender parity as of 2021.¹²⁷

Although women remain underrepresented in executive leadership roles, women's share of the C-suite among Russell 3000 companies has seen some improvement in the past decade.¹²⁸



Trends in Women Investors in Small Businesses

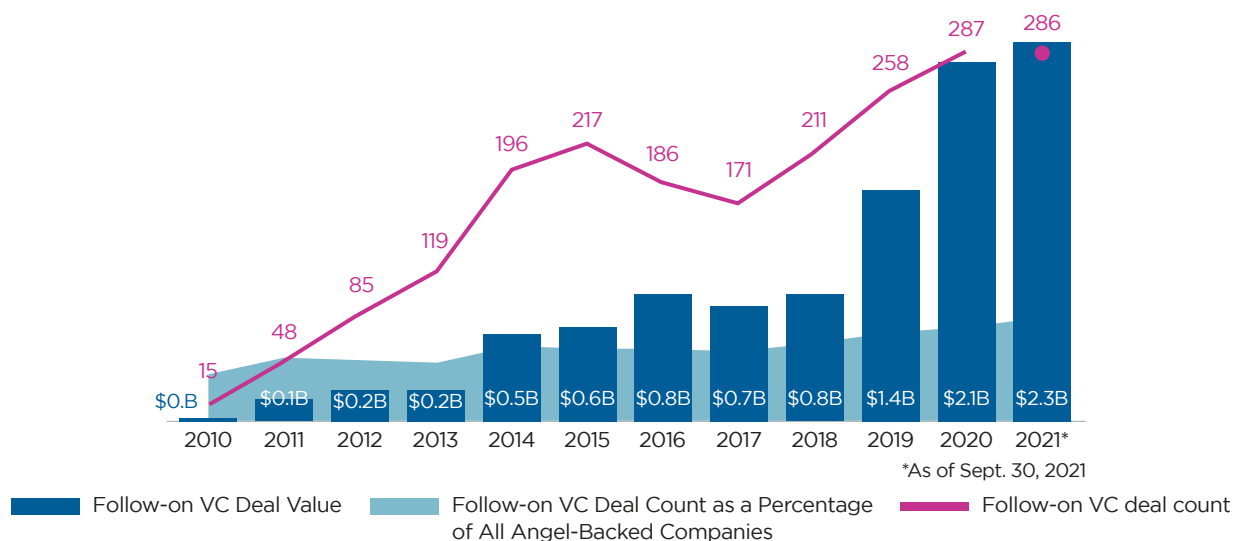
Women's representation among angel investors in 2020 remains largely unchanged since 2019.¹²⁹

29.5% of angel investors in 2020 were women (unchanged from 2019's level of 29.0%).

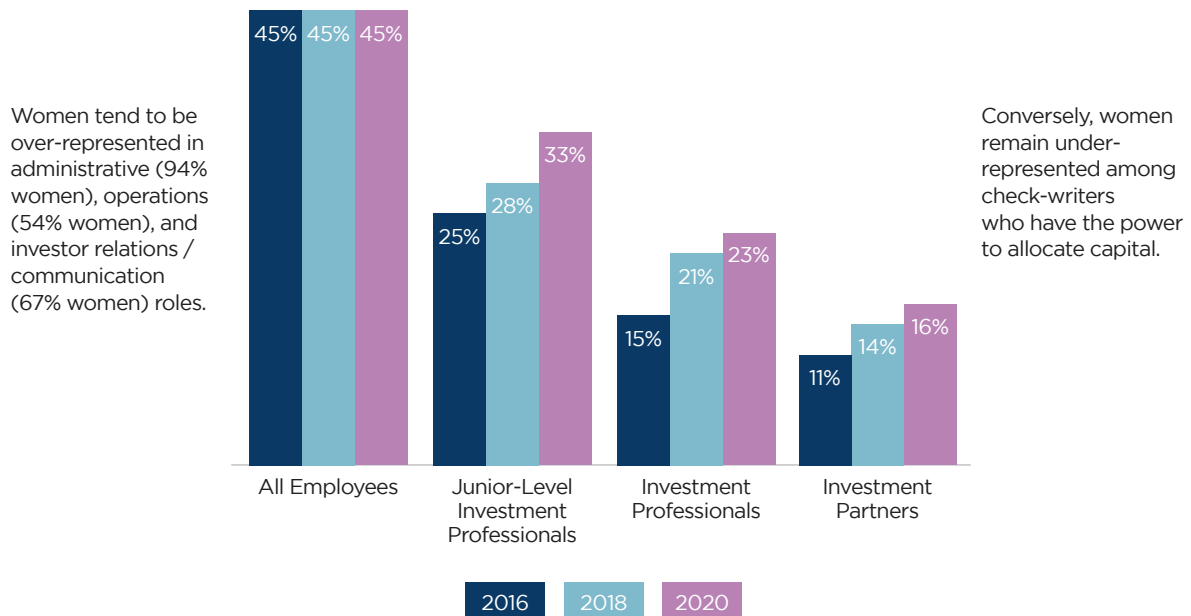


Women angels are backing companies roughly in proportion to their representation in the angel industry.¹³⁰

Companies backed by women angels are going on to raise increasing amounts of venture capital.¹³¹



Women remain underrepresented among decision-makers within the VC industry, though gender diversity has improved in the past 5 years.¹³²



Diversity among investment professionals directly impacts how the funds operate, and importantly the founders in whom the funds invest.¹³³



“

When you don't have enough diversity on the investing side of the table, you're very unlikely to see that diversity take place on the founder side.

SARAH KUNST, CLEO CAPITAL¹³⁴

Minority Business Owners and Investors

Precursors to Accessing Capital

Personal wealth dictates the financial starting line for many entrepreneurs' businesses, with funding often more accessible for those with homeownership and family assets.¹³⁵

The wide and persistent wealth gap across demographic groups¹³⁶ creates additional barriers to entry for many underrepresented entrepreneurs.¹³⁷



The wealth gap creates ripple effects across entrepreneurs' personal networks, which further exacerbates challenges accessing capital.



Hispanic/Latino entrepreneurs are 22% more likely than white entrepreneurs to rely on personal or family savings as a funding source.¹³⁹

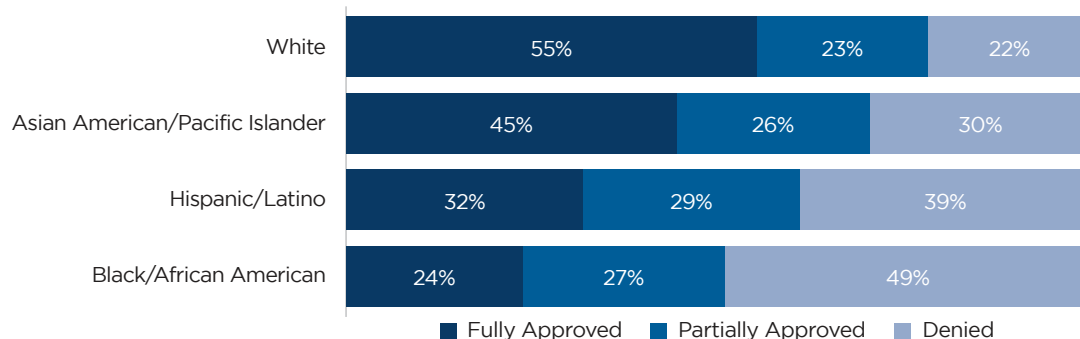


African American/Black entrepreneurs have fewer connections to banks, VC funds, and informal capital networks.¹⁴⁰



Hispanic/Latino entrepreneurs are more than twice as likely to find funding success when proactively networking with business organizations.¹⁴¹

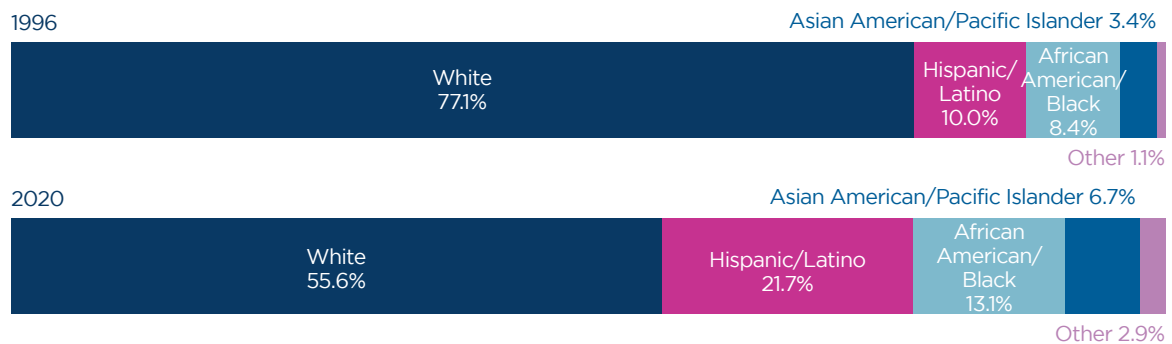
Minority entrepreneurs face greater challenges in accessing debt financing, including loans, lines of credit, and cash advances.¹⁴²



Business Formation and Ownership Trends

Entrepreneurial activity has meaningfully increased across minority groups in the past 15 years.¹⁴³

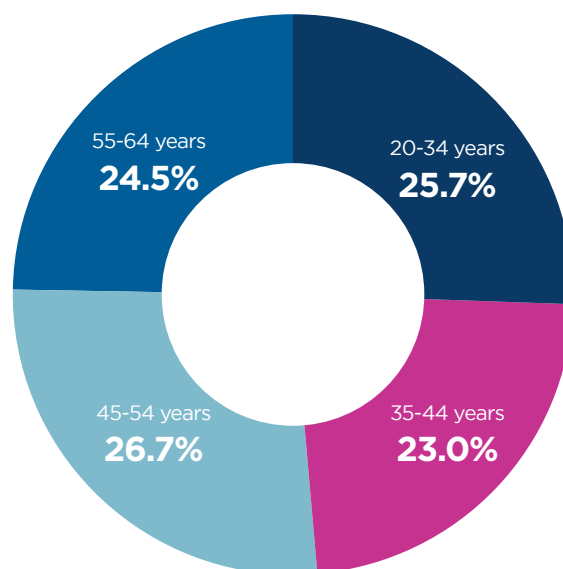
Hispanic/Latino entrepreneurship has seen the greatest growth of all groups, looking at both number of businesses as well as rate of revenue growth.¹⁴⁴



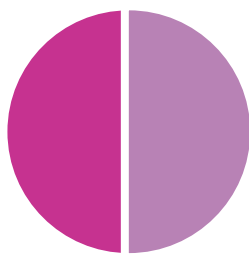
New entrepreneurs in 2020¹⁴⁵ also largely reflect population by race and ethnicity.¹⁴⁶



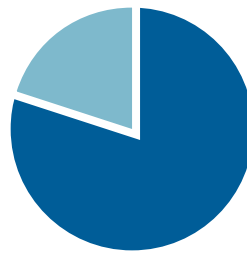
Contrary to the archetype of the 20-something entrepreneur that dominates the press, rates of entrepreneurship are evenly spread across age groups.¹⁴⁷



The COVID-19 pandemic has disproportionately impacted minority-owned businesses, many of which are overrepresented in service industries.



The five business sectors most affected by the pandemic generate almost **50% of the revenues** of Hispanic/Latino-owned businesses.¹⁴⁸

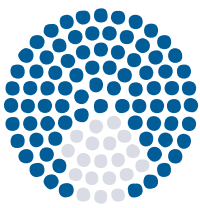


4 out of 5 small businesses

owned by Asian American/ Pacific Islanders report they are struggling financially from the pandemic.¹⁴⁹

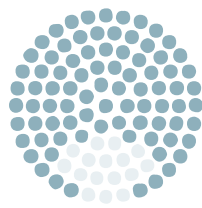
Among entrepreneurs over age 45, the decline in business ownership from January 2020 to January 2021 was more pronounced among minority populations.¹⁵⁰

Asian American/
Pacific Islander



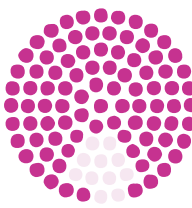
-19

African
American/ Black



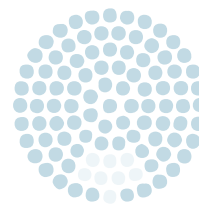
-16

Hispanic/Latino



-11

White



-8

Capital Raising Trends for Minority-Owned Businesses

Although underrepresentation of minority-founders persists, the investment yield rate among those who do seek angel funding has trended up.



Minorities constituted only

5.3%

of entrepreneurs seeking angel capital in 2020 (down from 9.3% in 2019),

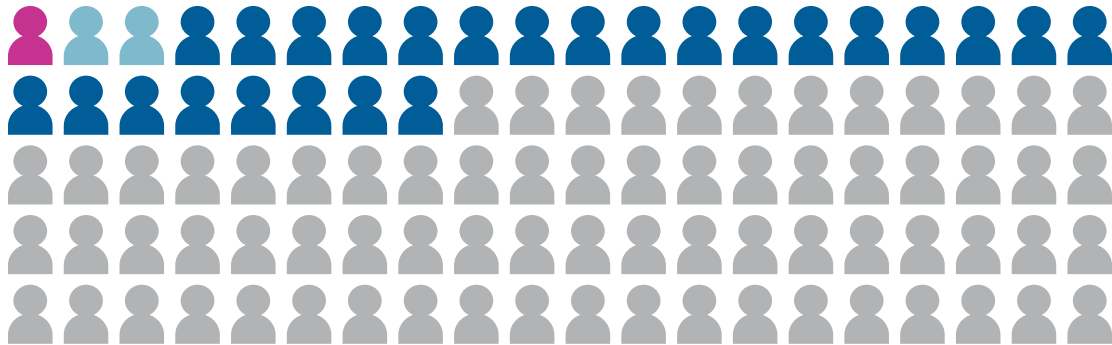


and had an investment yield rate of

33.0%

(up from 22% in 2019), compared to a baseline rate of 30.8%.¹⁵¹

Despite some progress in recent years, VC-backed companies are still predominantly led by white men.¹⁵²



28% of VC-backed founders are **Hispanic/Latino (1.3%)**, **African American/Black (1.7%)**, or **Asian American/Pacific Islander (25.2%)**, an aggregated increase from 23% in 2017.



The outlier model of investing in VC also typically results in a bias toward investing in homogeneous teams ... The people who can afford to take the biggest risks are also the people with the most privilege; they're not as concerned about providing for food, shelter and healthcare as economically stressed people are.

DAVID TETEN AND KATHERINE BOE HEUCK¹⁵³

LGBTQ+ founders also face challenges when raising capital, with many choosing not to “out” themselves to better pattern match investors’ expectations.¹⁵⁴



Though challenging to estimate, by one count, **less than 1%** of VC deals back LGBTQ+ founders.¹⁵⁵



40% of LGBTQ+ small business owners surveyed said raising capital is their **greatest business challenge**.¹⁵⁶



By one calculation, there is a **48% gap** in angel and VC funding actually going to LGBTQ+ founders and what should be achievable.¹⁵⁷

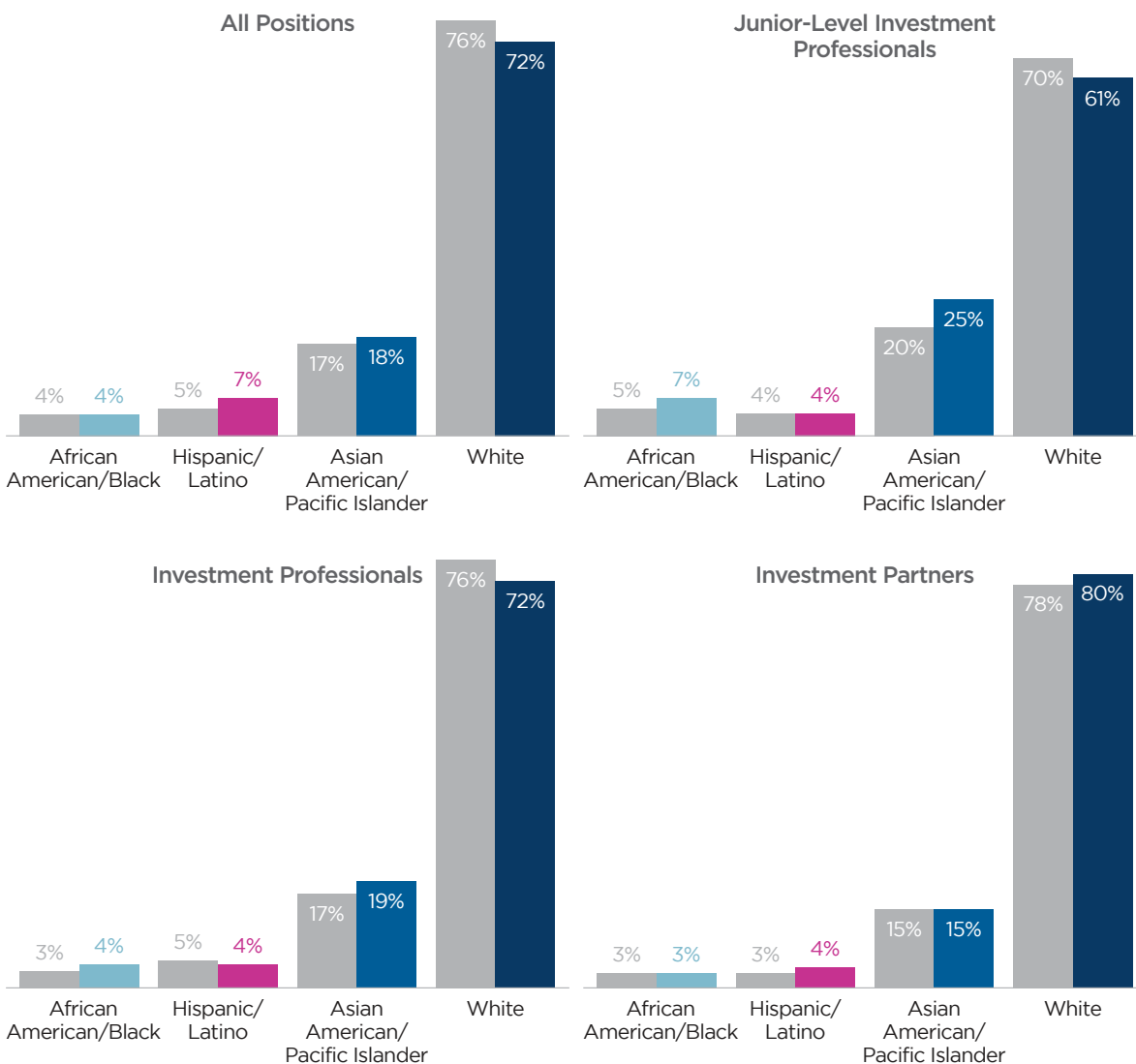
Minority Investors and Allies

Minorities remain vastly underrepresented among angel investors.



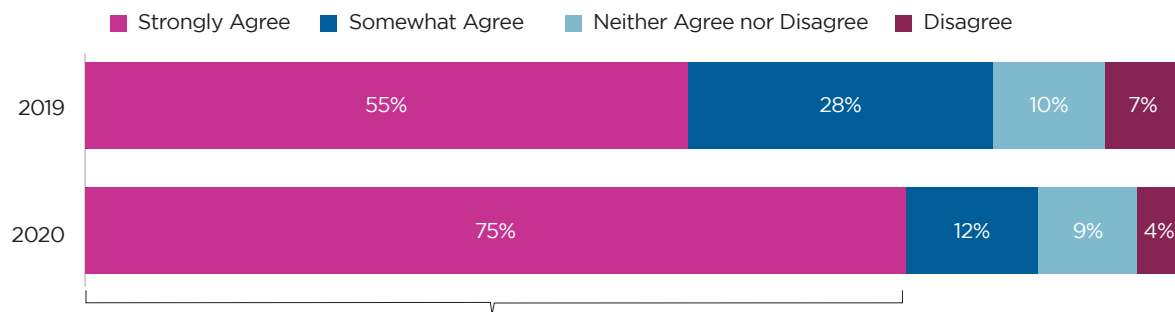
5.5% of angel investors in 2020 were minorities
(down from 2019's level of 7%).¹⁵⁸

Although minorities are still underrepresented among decision-makers within the venture capital industry, firms have shown some progress from 2018 (gray bars) to 2020 (colored bars) in increasing diversity.¹⁵⁹

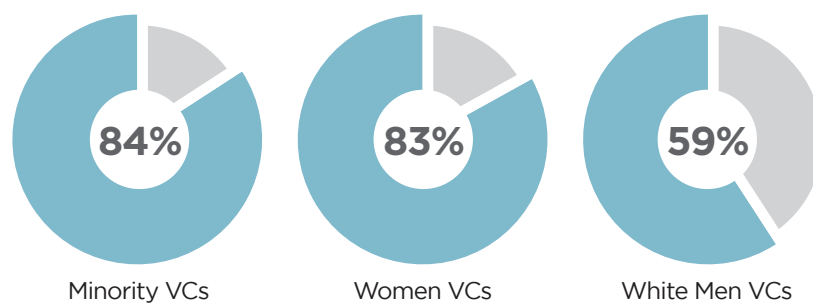


Investor sentiments about diversity are changing.

The year 2020 saw a sharp increase in the number of investors who agreed that it is possible to have an investment strategy that intentionally invests in women and minorities while still maximizing returns.¹⁶⁰



However, the breakdown of investors who strongly agree with the above statement skews towards women and minority VCs, who are underrepresented within the industry.¹⁶¹



Notably, almost all of the VCs who tracked their returns by demographic profile of founder reported that minority-founded company returns were performing on, or above, average, relative to the entire portfolio.¹⁶²

Shifting attitudes among VCs are beginning to impact hiring, funding, and strategic decisions, which should create ripple effects in diversity of funded ventures.

59%

of VCs say the Black Lives Matter movement has affected their investment strategy.¹⁶³

17%

of VCs expressed satisfaction with the number of minority entrepreneurs in their portfolio.¹⁶⁴

55%

of VC firms have recently brought on more women or minority LPs, fund managers, partners, or board members.¹⁶⁵

After a natural disaster, small businesses often experience direct expenses to renovate damaged property and equipment, as well as indirect expenses from the loss of revenue.¹⁶⁸

Small businesses are less likely to have cash reserves on hand, and more likely to face extreme challenges in response to even a month-long closure.



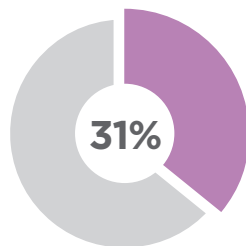
1 in 3

small business owners do not know if their business would survive if they were forced to close for more than a month.¹⁶⁹



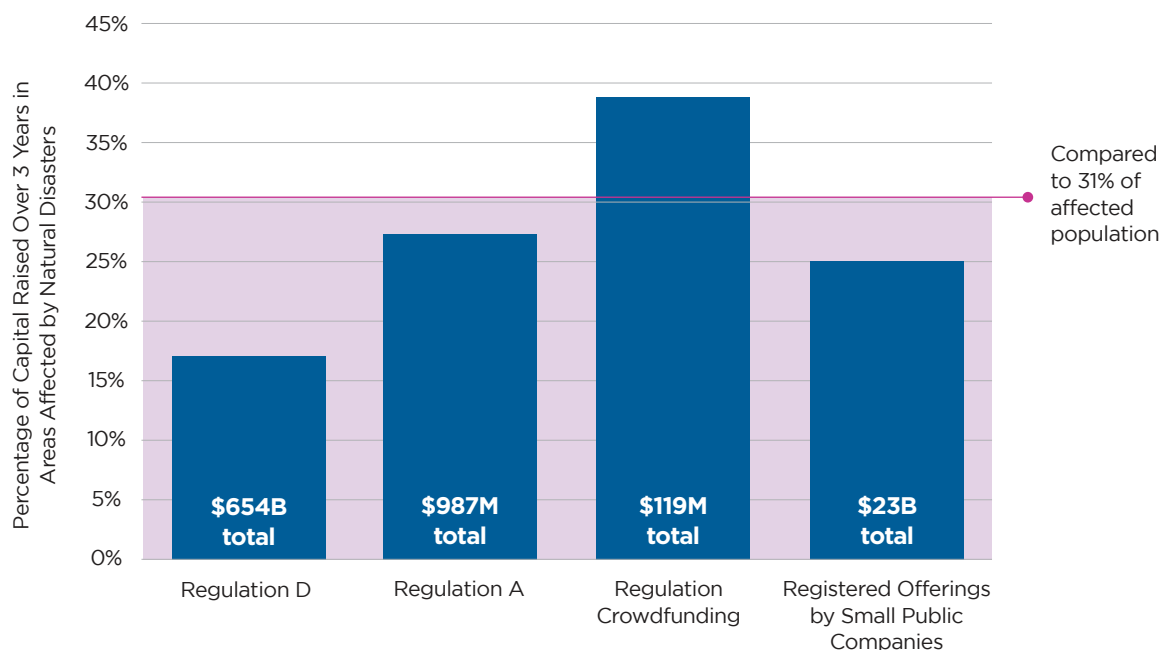
The average small business has **27 days** of cash flow buffer,¹⁷⁰ and for some, that number is closer to two weeks.¹⁷¹

How does the percentage of the population affected by natural disasters compare to the amount of capital being raised?



of the U.S. population¹⁷² lives in an area that was affected by a natural disaster over the three years ending June 30, 2021.¹⁷³

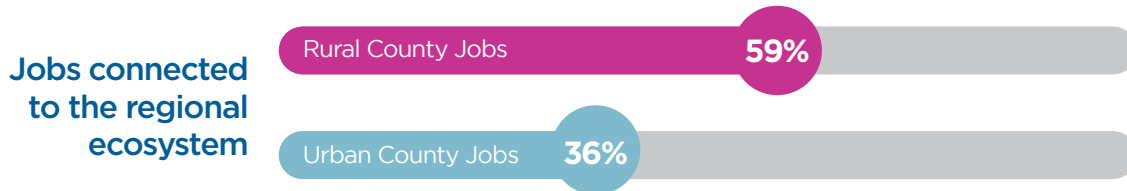
However, businesses in areas affected by natural disasters are generally raising less capital relative to the affected population, except with respect to offerings pursuant to Regulation Crowdfunding.¹⁷⁴



Rural Communities

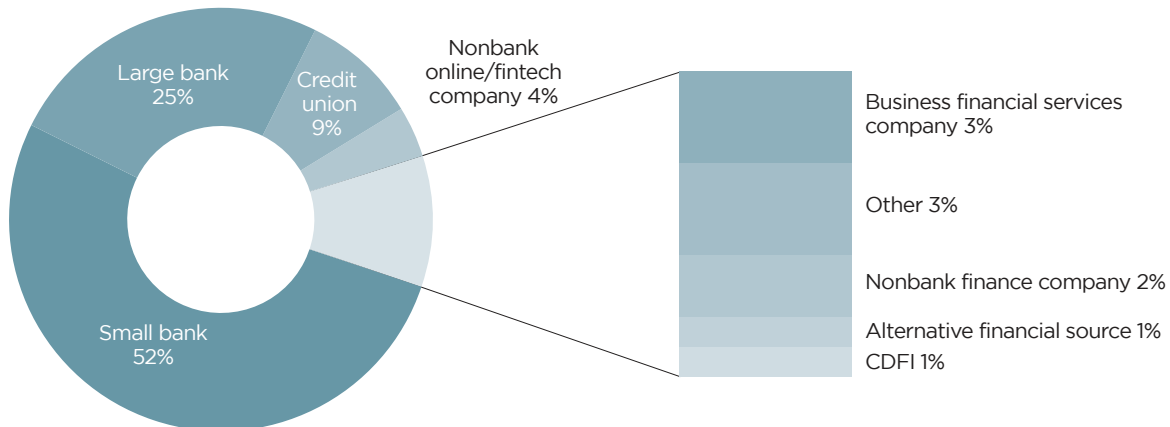
Job creation in rural communities relies more heavily on regional ecosystems

Economic activity in rural counties helps drive regional clusters that return economic opportunities back to local residents. This cycle is more pronounced in rural counties than in urban counties.¹⁷⁵



Small banks remain the primary source of capital for rural entrepreneurs

While rural entrepreneurs rely on a diverse array of traditional and nontraditional capital resources to meet their financing needs, small banks still lead as the primary source of capital in rural communities.¹⁷⁶



Rural business owners often view the involvement of investors through a different lens

Many rural business owners weigh additional variables in determining whether to seek capital from investors beyond mere capital needs, reflective of the close relationships between employers, employees, and their broader community, including:¹⁷⁷



Importance of establishing shared values with investors



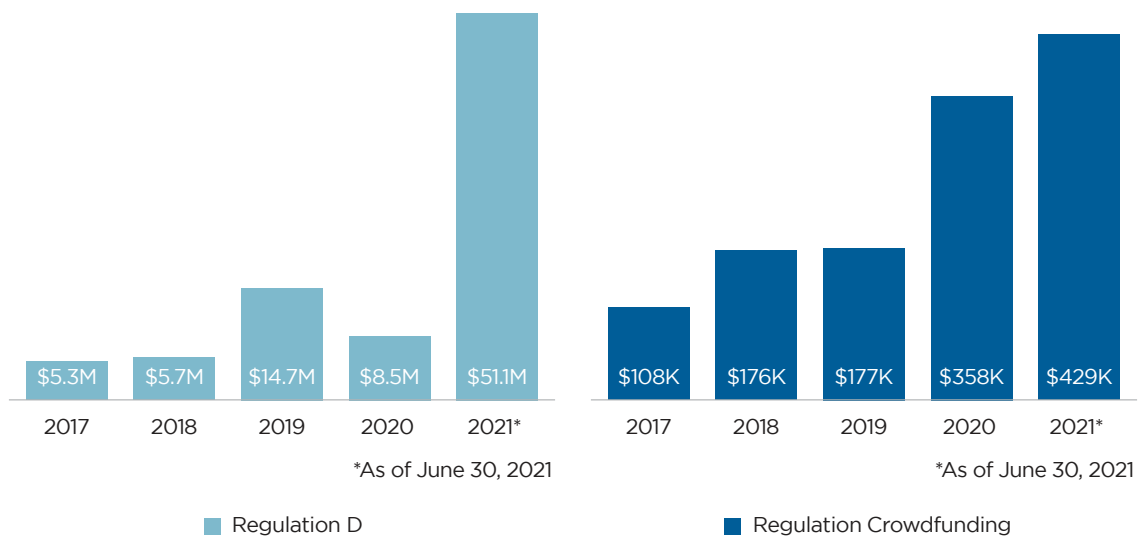
Prioritizing of continued support of the employees and community over profits



Unwillingness to sacrifice the personal lives of the owners or employees in exchange for growth

Rural businesses who seek investor capital are raising increasing amounts

Rural businesses are increasingly raising larger amounts of investment capital on average, including through Regulation Crowdfunding and Regulation D.¹⁷⁸



How does the rural population compare to the amount of capital being raised?



18%

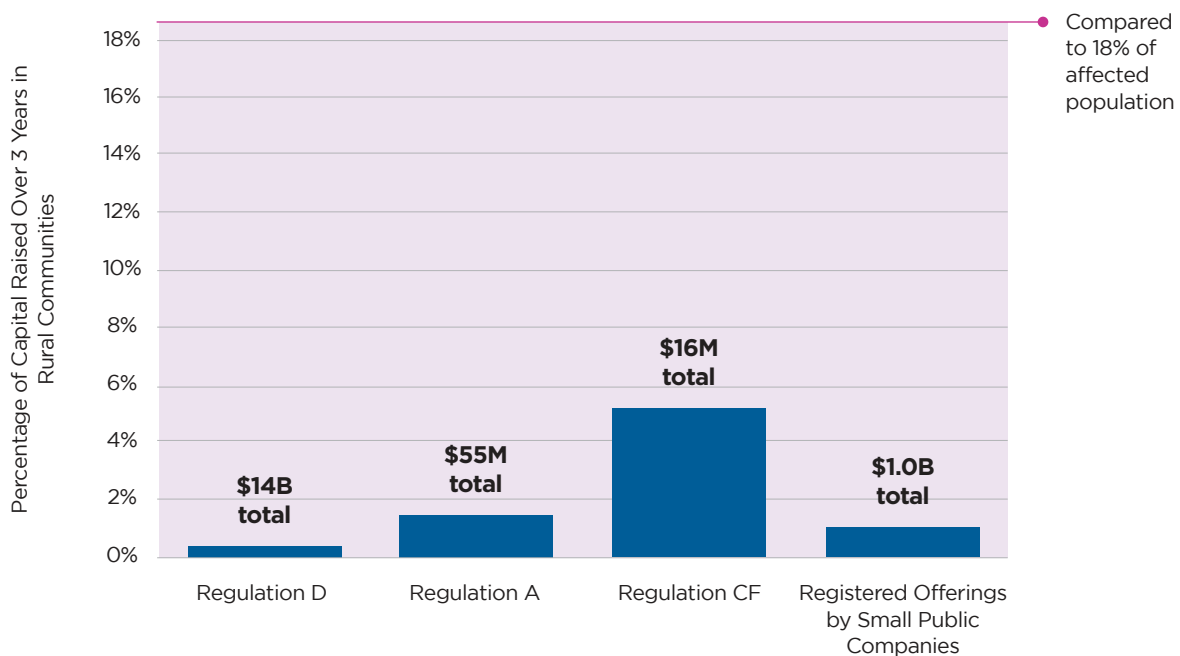
of the U.S. population
lives in rural areas.¹⁷⁹



16%

of small employer firms are
located in rural areas.¹⁸⁰

However, businesses in rural areas¹⁸¹ are raising less capital relative to the affected population over three years ending June 30, 2021:



This year the Office partnered with Alicia Robb, Ph.D. to measure capital raising activity in rural communities. [Download your copy of the report: “Rural Entrepreneurship and the Challenges Accessing Financial Capital: An Overview of Funding in Rural America.”](#)¹⁸²

Rural Entrepreneurship and the Challenges Accessing Financial Capital: An Overview of Funding in Rural America*

By Alicia Robb, Ph.D.

Next Wave Impact and the University of Colorado, Boulder

FINAL DRAFT
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SEPTEMBER





Policy Recommendations

The Office developed the following policy recommendations for Congress and the Commission based upon feedback received from small businesses and investors affected by our capital raising rules. We have distilled their feedback into four key areas for action addressing the most significant issues raised.

We recognize that for any complex issue, such as challenges surrounding capital formation, there are a multitude of potential solutions, and indeed multiple solutions may be needed to arrive at the impact sought. For each of the recommendations, we include background context, particular impact to demographic groups, notes on recent Commission action, and our proposed solution.

We welcome further engagement by Congress and the Commission in implementation of these solutions so that entrepreneurs and their investors together can bring innovations to market.

Entrepreneurs need support navigating complex securities laws.

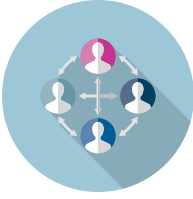


Background Context

All businesses need capital to create jobs, grow, and scale, no matter how small, from the corner coffee shop to the enterprise tech startup. Some businesses are funded by personal savings, debt financing, or retained business earnings, but those resources are inaccessible to many entrepreneurs, whether because of limited wealth, lack of operating history, or innovations that are pre-revenue.¹⁸³ Many of those entrepreneurs will look to investors to finance early-stage operations and development.

Even for the most technically sophisticated entrepreneur—whether a biomedical researcher commercializing a pharmaceutical patent, an app developer pioneering novel code, or an industrial innovator scaling a cleantech solution—the language of capital raising and the nuances of our complex rules are often inaccessible. Great entrepreneurial insight does not translate into fluency in almost a century of layered securities laws.

Most entrepreneurs find themselves in the dark when it comes to the rules of raising capital, reliant upon legal counsel to not only select an offering pathway that works for them, but to explain the nuanced rules to facilitate compliance. In other words: entrepreneurs who already find themselves cash-strapped must spend valuable—and often unavailable—resources just to understand their menu of options.



Demographic Impacts

Minority and women entrepreneurs are not on a level playing field when obtaining funding from investors, as we highlighted in our earlier State of Small Business Capital Formation section of this report. The proportion of capital raised by women-owned businesses pales in comparison to the capital raised by men-owned businesses.¹⁸⁴ Despite increasing rates of entrepreneurship in minority communities,¹⁸⁵ minority entrepreneurs continue to face challenges accessing investor capital from the earliest stages through later-stage VC,¹⁸⁶ leaving them financially constrained and unable to reach their full potential. For our capital markets to become inclusive, the art of capital raising must first become more accessible.



Recent Commission Action

In our [2020 Annual Report](#), we highlighted the need for targeted educational resources to support entrepreneurs and investors navigating the exempt offering framework.¹⁸⁷ We noted that educational resources should help users identify which options best fit their capital needs, risk tolerance, and long-term objectives.

Since then, the Commission has supported our Office's efforts to expand accessibility of capital raising resources by launching the following:

- [Capital Raising Hub](#) on sec.gov that targets a gap in accessibility of content on how to comply with securities laws when raising capital.
- [Cutting Through the Jargon](#) glossary of key terms that makes the language of capital raising more accessible to small business owners and their investors.
- [Navigate Your Options](#) interactive tool that explores regulatory pathways available to raise capital, through which users answer a series of questions to identify the most relevant pathways to raise capital based on their specific needs.
- [Capital Trends Maps](#) that provide data on where capital is being raised across the country under various offering pathways.
- [Emerging Fund Managers](#) series of virtual events to empower a new generation of investment decision makers and increasing diversity among capital allocators.

The resources were developed based upon feedback received directly from prospective users during outreach. We have engaged with small businesses, investors, and thought leaders in the market to highlight these new educational resources, and we continue to seek engagements with diverse audiences across the country. Notably, we encourage entrepreneurs and investors to reach out to our Office with suggestions on how we can build upon these resources.



Proposed Solution

Looking forward, additional resources are needed to equip entrepreneurs and their investors with capital raising tools to support a healthy investing ecosystem for both small businesses and their investors. Development of these resources should include:

- Engaging, digital tools to reach diverse audiences with accessible and plain language information, including short videos, infographics, and Q&A guides.
- Promotion in partnership with federal and state agencies to bolster the reach of the resources and others' efforts to promote capital raising and compliance.
- Partnerships with diverse groups of entrepreneurs and investors, including women, minorities, rural communities, communities impacted by natural disasters, and other underrepresented founders.

Additionally, it is critical that we maintain pathways for emerging companies to grow and scale via exempt offerings. As the Commission considers changes to the regulatory framework,¹⁸⁸ it is critical to consider barriers to entry for underrepresented founders and to avoid creating regulatory foot faults that impact the ability of founders to secure future rounds of financing as their businesses grow.

Many entrepreneurs may have goals of one day becoming a public company; others may have goals of creating a medium-sized business that supports their family and community, but not of the size and scale of a public company. For both sets of entrepreneurs, the capital they raise in the private markets is often the difference between reaching that next milestone and hiring additional employees, or having to close their doors.¹⁸⁹ They need well-functioning exempt offering pathways.

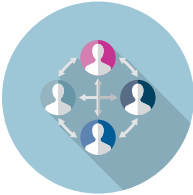
Founders need bridges from their personal networks to savvy investors.



Background Context

To build successful companies, startups need savvy investors who bring industry experience, customer connections, and strategic guidance. However, professional angels and venture capitalists are outside of many entrepreneurs' social and geographic networks, which can dramatically impact survival versus failure prospects for an early-stage company.¹⁹⁰ Developing solutions to bridge social and professional networks is critical for building more companies that succeed.

The securities laws are not clear, however, when it comes to that bridge-building capacity. In particular, there is a lack of clarity on the role of finders in facilitating introductions between founders and investors.¹⁹¹ Given the relatively low-dollar transaction sizes of early-stage capital, our Office regularly hears that registered broker-dealers are not helping bridge this gap.



Demographic Impacts

As we noted in our [2020 Annual Report](#), network challenges are magnified among women, minority, and rural founders, where social capital plays a critical role in startup success.¹⁹² The lack of access to networks of potential investors has an impact that extends well beyond capital raising to company survival and growth prospects, diversity among board leadership, recycled capital from entrepreneurs-turned-investors, and long-term wealth-building.



Recent Commission Action

In October 2020, the Commission [proposed an order](#)¹⁹³ that would permit natural persons to engage in certain limited activities involving accredited investors without registering with the Commission as a broker-dealer. The Commission received numerous comments in response, including a recommendation from the Commission's [Small Business Capital Formation Advisory Committee](#).¹⁹⁴ Most commenters agreed with the need to provide regulatory clarity that delineates the legal obligations of persons who bridge the networks between founders and investors. However, many commenting on the proposal identified concerns with the approach proposed by the Commission and suggested alternatives for the Commission to consider. Since then, the Commission has not taken further action on the proposal, and providing regulatory clarity for finders is not in the Commission's current regulatory agenda.¹⁹⁵



Proposed Solution

For decades the market has asked for clarity about the legal obligations of finders. A clear framework will support compliance with securities laws, increase investor protections, and level the playing field for founders who lack access to networks of sophisticated investors. We encourage Congress and the Commission to consider the comments the Commission received in response to the proposed order and to finalize a regulatory framework that helps bridge the networks between social and financial capital so that access to investment capital can be less about *who* you know, and more about what you know and the innovations you bring to bear.

Diversifying capital allocators requires supporting emerging fund managers.

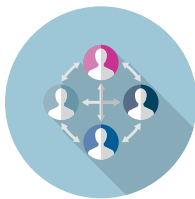


Background Context

When businesses look for funding beyond friends and family or their local angel network, they very often are turning to private funds of sophisticated pooled capital, such as VC funds. Founders looking for seed and early-stage capital often struggle to raise financing for their smaller, earlier rounds. Many founders refer to the period between the early rounds of financing and the Series B round as the “valley of death,” as there are fewer investors who are able to participate in the typically more regional, smaller rounds of \$10 million before the large VCs come to the table for a Series B round.

While the past year has been a banner year for capital raising by funds in general, the vast majority of that capital is concentrated into large, established private funds.¹⁹⁶ Generally speaking, the larger the fund size, the larger their target investment check size, so that they can actively manage a small portfolio of companies. This has the result of either pushing valuations higher, which has happened across the technology industry, or pushing aside earlier-stage, smaller deals in favor of later-stage, more mature companies.

Emerging fund managers and their smaller funds are more likely to invest in a more diverse pool of entrepreneurs, as well as entrepreneurs located in areas not traditionally served by more established fund managers. However, funds raised by emerging fund managers are on the decline,¹⁹⁷ as the market faces concentration of investment-decision making in the hands of a few.



Demographic Impacts

The VC industry—and the investment decision-makers at the firms—are notoriously homogenous across racial, ethnic, and gender lines.¹⁹⁸ While we have seen modest gains in diversity of representation among “check writers” at funds, the population of decision-makers does not reflect the population of entrepreneurs seeking capital.¹⁹⁹

Diversity among funders directly impacts diversity among the funded. While many sophisticated investors recognize the bias inherent in pattern-matching to the archetype of a successful, young, white, male entrepreneur, it is critical that we empower diverse investment decision-makers who can support and invest in solutions to the problems that they too face.



Recent Commission Action

Over the last year our Office’s [Emerging Fund Manager series](#) explored solutions to help address some of the challenges emerging fund managers face breaking into the industry, including the financial toll that launching a new fund can place on the fund manager personally, the difficulties that come with having a limited track record, and the impact of personal network on capital raising prospects. These challenges are magnified for women and minority emerging fund managers.

The Commission has broadly supported diversity-related initiatives, including through its different advisory committees, and has encouraged continued engagement and ideas to improve the resources available to underrepresented and emerging fund managers and their limited partners.²⁰⁰



Proposed Solution

In our [2020 Annual Report](#), we encouraged Congress and the Commission to explore regulatory solutions to support smaller, regional funds that support their ecosystems through locavesting. We support a number of policy solutions raised during our [Emerging Fund Manager series](#) and recommended by the [SEC Small Business Capital Formation Advisory Committee](#), including:

- Improving the utility of the “qualifying venture capital fund” exemption in Section 3(c)(1) of the Investment Company Act of 1940 by increasing the current \$10 million limit on the aggregate amount of capital contributions and uncalled committed capital.²⁰¹

Assuming a generous “2 and 20” fee structure by a fund,²⁰² a \$10 million qualifying venture capital fund would be hamstrung to operate on \$200,000 per year, inclusive of salaries, compliance, diligence, and portfolio management costs, an amount so low it functionally sets these small funds up to fail. Increasing the qualifying venture capital fund limits would equip emerging fund managers and smaller, regional funds with a pathway to raise meaningful capital, while also covering their operational costs without charging an outsized fee to investors.

- Amending the “venture capital fund” definition under Rule 203(l)-1 of the Investment Advisers Act of 1940 to permit VC funds to invest in other VC funds in satisfaction of the “qualifying investment” requirements of the rule.

Amending the venture capital fund definition under the Advisers Act would allow larger—and often more geographically concentrated—funds to invest in emerging fund managers who write smaller checks, both increasing the diversity of investment decision-makers and accessibility of smaller check sizes.

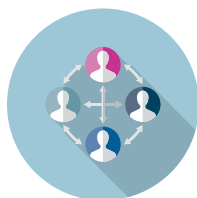


Background Context

This has been a banner year for IPOs, with record amounts raised in public offerings and record numbers of companies going public compared to recent years.²⁰³ VC-backed companies continue to be the majority of exchange-listed IPOs,²⁰⁴ reflecting the critical nature of pre-IPO capital raised in the private markets that prepares companies for the public markets. While the headlines are often focused on the offerings of large public companies, smaller public companies have also seen growth in equity offering activity in the last year.²⁰⁵

Our Office is acutely aware of the importance of not only the process of going public, but also what it takes to remain a public company. Smaller public companies continue to experience declining research coverage, challenges raising capital from institutional investors, and a less liquid market for their investors compared to the market for larger companies, in addition to compliance costs.²⁰⁶ Many aspects of our regulatory structure were originally targeted at the largest of public companies, and when applied to smaller public companies often demand disproportionate financial and human capital resources.

The past year has seen rising interest from many investors in additional disclosures on environmental, social, and governance (ESG) matters,²⁰⁷ with many public companies scrambling to keep pace with demands. Much of the data and interest in this space, particularly with respect to environmental and climate issues, has focused on larger public companies.



Demographic Impacts

Stakeholders—including investors, exchanges, employees, and customers—are increasingly driving public companies to focus on diversity and inclusion both internally within their leadership and workforce, as well as externally in their business operations. However, the leadership taking companies public remains largely homogeneous, a reflection of the social and financial capital available to entrepreneurs pre-IPO that ripples into the public markets.²⁰⁸ The challenges our Office highlighted above with respect to diversity among entrepreneurs accessing capital²⁰⁹ and decision-makers writing checks²¹⁰ directly impacts who carries the title of CEO on opening day and who sits around the boardroom guiding that company's decisions.



Recent Commission Action

In our [2020 Annual Report](#), we encouraged Congress and the Commission to consider market innovations that could have the effect of encouraging more companies to go public, and the past year certainly was a banner year for IPOs.²¹¹

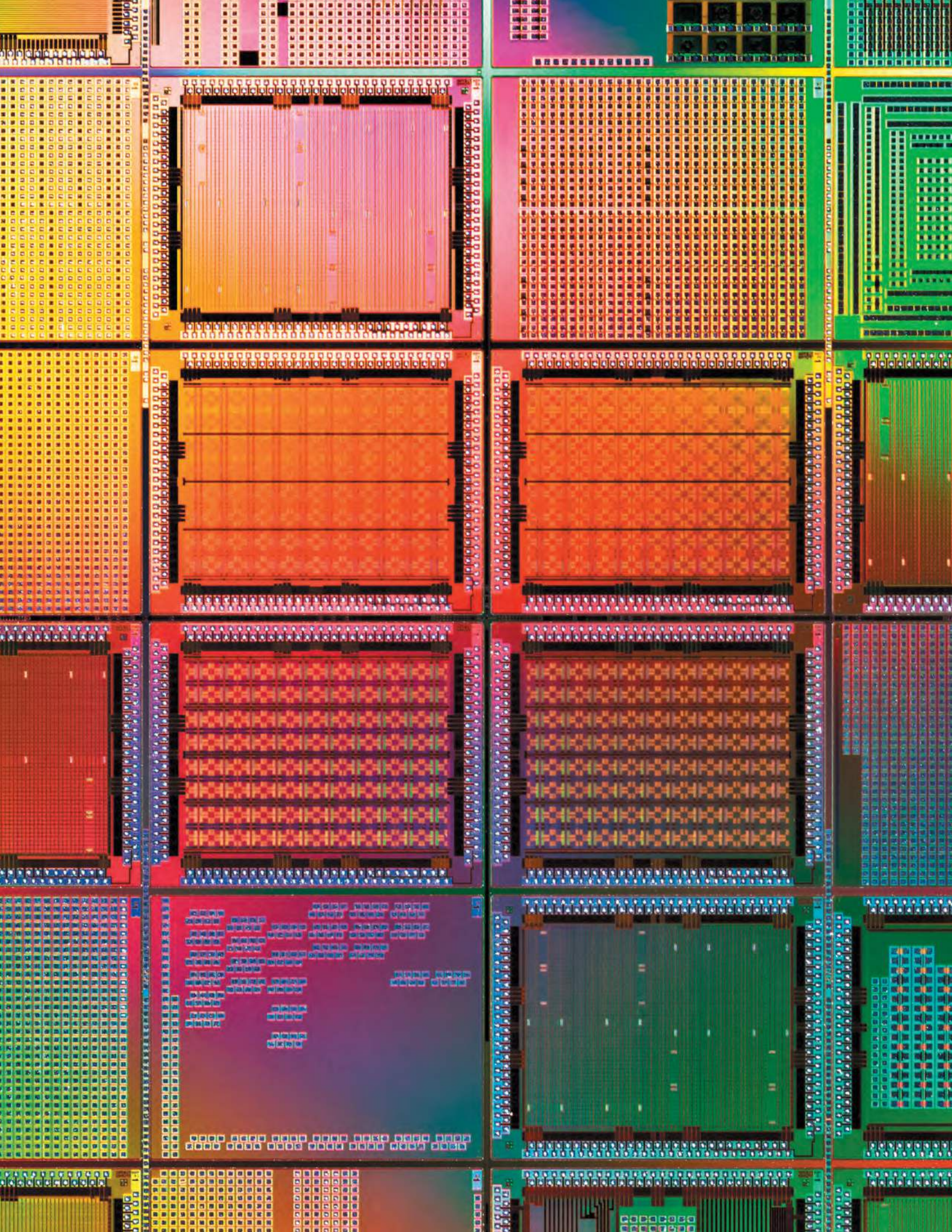
In response to calls for more ESG disclosures, the Commission indicated in its [regulatory flexibility agenda](#) that it may propose additional disclosure requirements relating to climate risk, human capital (including workforce diversity and corporate board diversity), and cybersecurity risk.²¹² The Commission has also indicated interest in further refining the disclosures made by SPACs bringing companies public.



Proposed Solution

The vibrancy of our capital markets depends on having companies of varying sizes, from micro-cap to mega-cap, to provide investors with meaningful options for investment, the trademark of our public markets.

In developing rules to improve disclosures to investors by public companies, it is critical to be mindful of how and whether our rules are promoting an environment that fosters smaller public companies going and remaining public. We support efforts to continue tailoring the disclosure and reporting framework to the complexity and size of operations of companies, either by scaling obligations or delaying compliance for the smallest of the public companies, particularly as it pertains to potential new or expanded disclosure requirements.



Small Business Capital Formation Advisory Committee FY2021 Summary

The [Small Business Advocate Act](#) also established the SEC's [Small Business Capital Formation Advisory Committee](#). The Committee is designed to provide a formal mechanism for the Commission to receive advice and recommendations on Commission rules, regulations, and policy matters affecting small businesses, from emerging, privately-held companies to publicly-traded companies with less than \$250 million in public market capitalization; trading in securities of such companies; and public reporting and corporate governance of such companies. The Office provides administrative support for the Committee, which otherwise functions independently.

The Committee's membership includes companies and investors from across a diverse set of experiences, industries, geographies, and company life cycle stages. In FY2021, Andrea Seidt succeeded Michael Pieciak and Melanie Senter Lubin's service as the North American Securities Administrators Association's representative. Bailey DeVries succeeded William Manger as the Small Business Administration's representative shortly after the end of FY2021. The Commission is grateful for their service and commitment to small businesses and their investors.

The members of the Committee as of the end of FY2021 were as follows:



CARLA GARRETT, *Chair*
Corporate Partner,
Potomac Law Group PLLC
Washington, DC



YOUNGRO LEE, *Assistant Secretary*
CEO and Co-Founder,
NextSeed
Houston, TX



JEFFREY M. SOLOMON,
Vice Chair
Chief Executive Officer, Cowen, Inc.
New York, NY



KESHA CASH
Founder and General Partner,
Impact America Fund
Oakland, CA



GREGORY YADLEY, *Secretary*
Partner, Shumaker, Loop &
Kendrick, LLP
Tampa, FL



GREG DEAN*
Senior Vice President of the Office
of Government Affairs, FINRA
Washington, DC



ROBERT FOX

National Managing Partner,
Professional Standards Group,
Grant Thornton LLP
Chicago, IL



POORVI PATODIA

CEO and Founder,
Biena Snacks
Allston, MA



STEPHEN GRAHAM

Co-Chair, Fenwick & West LLP's Life
Sciences Practice
Seattle, WA



JASON SEATS

Chief Investment Officer,
Techstars
Austin, TX



SARA HANKS

CEO and Co-Founder,
CrowdCheck, Inc.
Alexandria, VA



ANDREA SEIDT*

Ohio Securities Commissioner of
the Ohio Department of Commerce
Columbus, OH



BRIAN LEVEY

Chief Business Affairs and Legal
Officer, Upwork Inc.
Santa Clara, CA



MARC OORLOFF SHARMA*

Chief Counsel of the Office of the
Investor Advocate, U.S. Securities
& Exchange Commission
Washington, DC



SAPNA MEHTA

General Counsel & Chief
Compliance Officer, Rise of
the Rest Seed Fund; Associate
General Counsel, Revolution
Washington, DC



HANK TORBERT

President,
AltaMax, LLC
New Orleans, LA



MARTHA LEGG MILLER*

Director, Office of the Advocate for
Small Business Capital Formation,
U.S. Securities & Exchange
Commission
Washington, DC



SUE WASHER

President and CEO, Applied Genetic
Technologies Corporation
Gainesville, FL



CATHERINE MOTT

Founder and CEO of BlueTree
Capital Group, BlueTree Allied
Angels, and BlueTree Venture Fund
Pittsburgh, PA

*Committee members include the SEC's Advocate for Small Business Capital Formation and three non-voting members appointed by each of the SEC's Investor Advocate, the North American Securities Administrators Association (NASAA), and the Small Business Administration, as well as an observer appointed by the Financial Industry Regulatory Authority (FINRA).

Summary of Activities

The Committee met virtually four times during FY2021. Materials from the meetings, including agendas, transcripts, webcasts, and presentations, are available on the Committee's [webpage](#).

Meeting Date	Agenda Topics
November 9, 2020	Proposed Conditional Exemption for Finders; COVID-19 Updates and Discussion
January 29, 2021	Pulse of the Public Markets; Compensatory Offerings for Gig Economy Workers
April 30, 2021	Increasing Capital Access for Underrepresented Founders and Investors
September 27, 2021	The Changing Dynamics Pre-IPO and Going Public



Committee Recommendations

During FY2021, the Committee put forward the following two recommendations to the Commission:

Encouraging Small, Regional Funds

April 30, 2021

The Committee explored ways to build upon its [August 2020 findings](#) by encouraging the Commission to improve access to capital for underrepresented founders and investors, including women, minorities, and founders outside of prominent tech hubs. In homing in on solutions, the Committee noted the following:

1. Recent trends show that many companies in established technology ecosystems are successful in raising capital. However, those figures leave out many entrepreneurs in other areas of the country and industries who struggle to raise the capital needed to grow and scale. The challenges are particularly acute for companies who are pre-revenue, making bank capital largely inaccessible. In particular, founding teams outside of tech hubs struggle to raise Series A capital, typically in the \$3 million to \$10 million range, after which point companies can more readily attract Series B capital from growth-oriented investors.
2. Pattern matching—or the process of making investment decisions that replicate patterns of who a successful entrepreneur has looked like in the past—perpetuates a cycle that has concentrated capital in limited geographies, ethnicities, genders, and educational backgrounds. Women and minority founders continue to struggle to raise capital and spend more time raising rounds of funding, relative to their White, male counterparts.
3. Many larger institutional investors express interest in supporting diversity, equity, and inclusion through investments in emerging fund managers and underrepresented founders. However, the combination of their minimum investment requirements (e.g., \$15 million to \$20 million) coupled with their maximum exposure within a single fund (e.g., 10% of the fund's AUM) functionally rules out direct investments by institutional investors in smaller, emerging funds, including regional Seed and Series A funds, which have the potential to meaningfully impact diversity of entrepreneurs raising capital.
4. Early-stage investors play an active role with their portfolio companies by providing hands-on support to founders, participating in board meetings, and supporting customer attraction strategies. Proximity to portfolio companies changes how early-stage investors evaluate investment opportunities. Additionally, the number of companies that the investor can actively mentor limits the number of investments that they can make. As a result, larger venture funds tend to invest larger amounts in a handful of later-stage companies, while smaller funds tend to invest smaller amounts in

a proportionate handful of earlier-stage companies. A fund of funds model—where a larger fund invests in smaller, regional funds—could unlock capital otherwise competing for late-stage allocations and benefit smaller companies in emerging entrepreneurial ecosystems. However, the limitations on exempt reporting advisers’ qualifying investments currently make this structure impracticable given the other competing demands on the 20% non-qualifying basket, including public offering commitments and secondary liquidity for founding teams.

5. First-time fund managers and smaller funds are declining in number and size, threatening access to the earliest stage capital that is catalytic to new companies’ success. For emerging fund managers, the ability to pool more investors in a fund presents a promising pathway to raise a more impactful fund, while also offering diversification that decreases portfolio risk for angel investors who would otherwise be investing independently. However, the current qualified venture capital fund size limit of \$10 million under Section 3(c)(1) of the Investment Company Act of 1940 is too low for a viable fund to cover its operational costs without charging an outsized fee to its investors.

In light of the foregoing observations, the Committee recommends the following changes:

- 1) With respect to the “qualifying venture capital fund” exemption in Section 3(c)(1) of the Investment Company Act of 1940:
 - a. increase the current \$10 million limit on the aggregate amount of capital contributions and uncalled committed capital to \$150 million; and
 - b. increase the number of permitted beneficial owners from 250 to 600.
- 2) Amend the “venture capital fund” definition under Rule 203(l)-1 of the Investment Advisers Act of 1940 to permit venture capital “fund of funds” investments by treating an investment in another venture capital fund, which itself meets the requirements of Rule 203(l)-1, as a “qualifying investment.”

Relevant Commission Action

The Commission supports efforts to improve diversity among fund managers and entrepreneurs who raise capital. In the spring of 2021, the SEC’s Small Business Advocacy office, in partnership with other SEC offices and divisions, launched a “[Cutting Through the Jargon](#)” glossary to reduce barriers to entry for underrepresented and emerging investors and entrepreneurs and to improve accessibility of compliance content. The Office also contemporaneously launched an Emerging Fund Manager virtual event series, exploring the role of emerging fund managers and their investors in funding underrepresented founders across the country and empowering a new generation of investment decision-makers.

“Qualifying venture capital fund” exemption in Section 3(c)(1)

The Commission has noted that any amendments to Section 3(c)(1) to change the \$10 million cap or to change the number of investors allowed would require Congressional action.²¹³

By way of background, a 3(c)(1) fund is a type of pooled investment vehicle that is excluded from the definition of “investment company” under the Investment Company Act of 1940 (1940 Act) because it has no more than 100 beneficial owners and otherwise meets criteria outlined in Section 3(c)(1) of the 1940 Act. 3(c)(1) funds are often used by venture capital firms and other early-stage investors who pool capital for investment in startups.

“Qualifying investments” and the “venture capital fund” definition under Rule 203(l)-1

In the adopting release defining “qualifying investment,” the Commission discussed the possibility of expanding the definition to include secondary purchases and investments in other venture capital funds, but ultimately decided that such investments should be made pursuant to the 20 percent limit for assets that are not “qualifying investments.”²¹⁴ Since then, the Commission has noted that the Division of Investment Management issued guidance relating to the definition of “venture capital fund” to clarify whether certain fund structures or actions could jeopardize a venture capital fund adviser’s ability to qualify as an exempt reporting adviser.²¹⁵

By way of background, an investment adviser to venture capital funds may qualify as an exempt reporting adviser that is not required to register with the SEC if the fund invests at least 80% of its assets in “qualifying investments” under Rule 203(l)-1 under the Investment Advisers Act of 1940.²¹⁶ A “qualifying investment” generally consists of any equity security issued by a qualifying portfolio company that is directly acquired by a qualifying fund and certain equity securities exchanged for the directly-acquired securities.

Finders

November 9, 2020

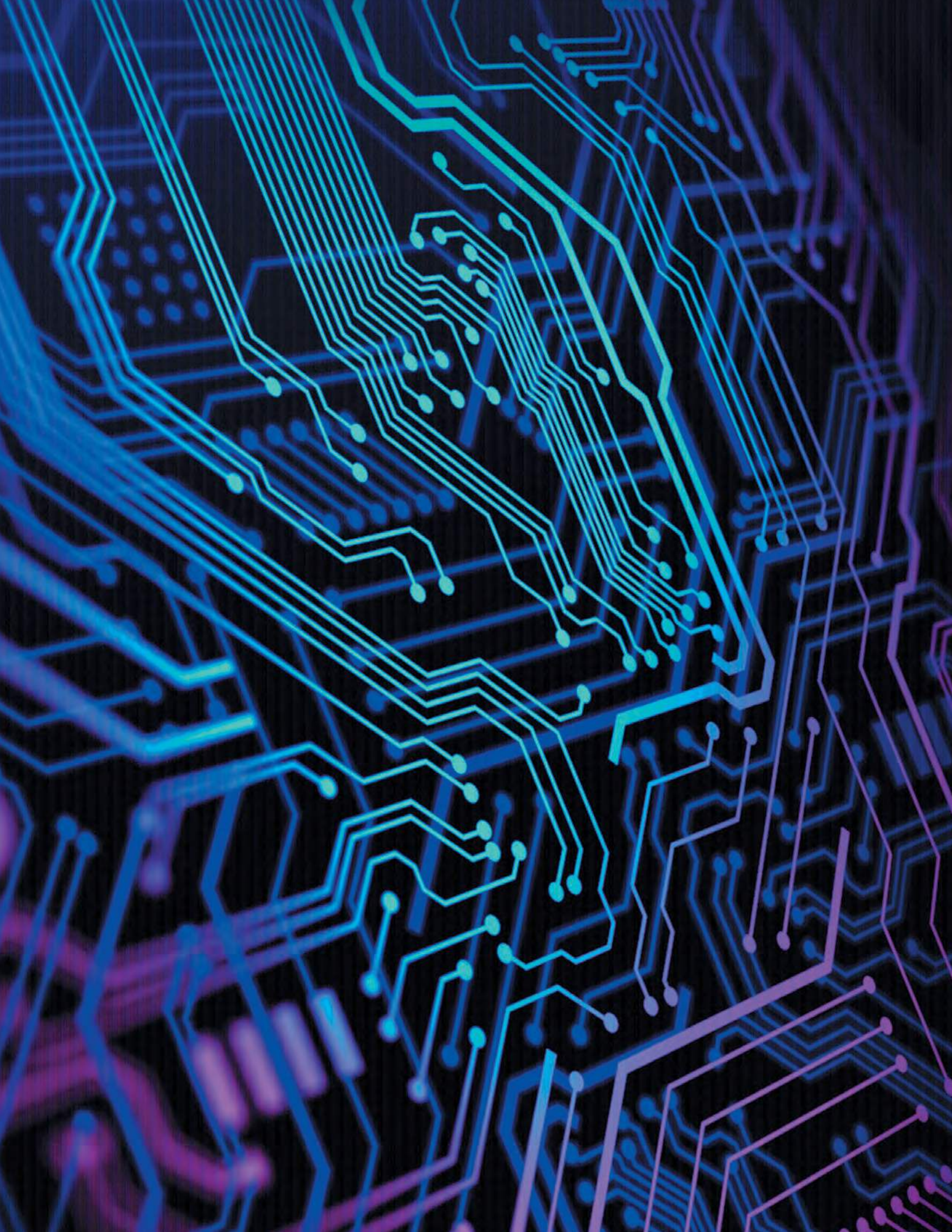
On October 7, 2020, the Commission [proposed](#) a new limited, conditional exemption from broker registration requirements for “Finders” who assist companies with raising capital in private markets from accredited investors. In order to promote small business capital formation, especially underrepresented businesses (such as minority owned and women owned businesses) and businesses that are not in regions with robust capital raising networks, the Committee supports a framework to permit certain Finders to engage in limited capital raising activities involving accredited investors with the following principles in mind:

- 1) The framework should be kept simple.
- 2) The framework should keep out bad actors.
- 3) The Commission should consider requiring a notice filing for all Finders, which includes information on fees charged for Finders’ services.
- 4) The Commission should work with state securities regulators to provide additional certainty for market participants with coordination among the states and the Commission.
- 5) It is important that Finders and Issuers know the rules on how Finders can assist with capital formation for small businesses.
- 6) The Commission should consider a blanket exemption for Finders for offerings under a certain size.
- 7) The Commission should consider the issue of fees to Finders, including the reasonableness around Finders’ fees and/or limits on the amount of Finders’ fees.
- 8) The Commission should add clarity on prohibited and permissible activities. For example, the contact restrictions, the one time per year, and the natural person requirements in the proposal may be too limiting.
- 9) The Commission should clarify whether broker-dealers are allowed to pay Tier 2 finders that are non-associated persons.

Relevant Commission Action

The Advisory Committee’s recommendation was made following the Commission’s October 7, 2020 proposed exemptive order that would permit natural persons to engage in certain limited activities involving accredited investors without registering with the Commission as a broker dealer.²¹⁷ In connection with that proposal, the Commission requested public comment on all aspects of the proposed exemption. Finalizing the proposal is not included in the Commission’s current regulatory agenda.²¹⁸





End Notes

- 1 The SEC conducts the Forum annually and prepares a report in accordance with the Small Business Investment Incentive Act of 1980 [15 U.S.C. 80c-1 (codifying section 503 of Pub. L. No. 96-477, 94 Stat. 2275 (1980))].
- 2 See Office of the Advocate for Small Business Capital Formation Annual Report for Fiscal Year 2020, at 66, *available at* <https://www.sec.gov/files/2020-oasb-annual-report.pdf>.
- 3 This graphic is based on DERA data. This graphic depicts amounts reported or estimated as raised from July 1, 2020 through June 30, 2021. Data on offerings under Regulations D and Crowdfunding is based on information reported by companies and was collected from EDGAR filings (new filings and amendments) on Forms D and C, respectively. Data on registered offerings was collected from Thomson Financial's SDC Platinum database. For offerings under Regulation Crowdfunding, except where specified otherwise, estimates of the number of offerings are based on offerings completed during this period as shown on progress updates on Form C-U; estimates of amounts raised are based on proceeds reported in progress updates filed on Form C-U during the report period. For offerings under Regulation A, except where specified otherwise, estimates of the number of offerings are based on offerings qualified during this period, excluding post-qualification amendments; estimates of amounts raised are based on proceeds reported in filings made during the report period. Capital raised is based on information reported by companies in Forms 1-Z, 1-K, 1-SA, 1-U, and offering circular supplements pertaining to completed and ongoing Regulation A offerings and post-qualification amendments, and for companies whose shares have become exchange-listed, information from other public sources. Estimates represent a lower bound on the amounts raised given the time frames for reporting proceeds following completed or terminated offerings and that offerings qualified during the report period may be ongoing. For the offerings that permit pooled investment funds, such as Rule 506(b) and (c) of Regulation D and registered offerings, the data includes offerings conducted by pooled investment funds.
- 4 "Other exempt offerings" includes estimated amounts raised under Section 4(a)(2), Regulation S, and Rule 144A for calendar year 2020. The data used to estimate the amounts raised in 2020 for other exempt offerings includes: (1) offerings under Regulation S that were collected from Thomson Financial's SDC Platinum service; and (2) resale offerings under Rule 144A that were collected from Thomson Financial SDC New Issues database, Dealogic, the Mergent database, and the Asset-Backed Alert and Commercial Mortgage Alert publications, to further estimate the exempt offerings under Section 4(a)(2) and Regulation S. We include amounts sold in Rule 144A resale offerings because those securities are typically issued initially in a transaction under Section 4(a)(2) or Regulation S but generally are not included in the Regulation S data identified above. These numbers are accurate only to the extent that these databases are able to collect such information and may understate the actual amount of capital raised under these offerings if issuers and underwriters do not make this data available. The data on Rule 144A debt offerings from Mergent is available only through October 26, 2021. We have extrapolated the data to obtain a full calendar year. We do not yet have data to provide an estimated amount raised under Section 4(a)(2), Regulation S and Rule 144A for the 12 month period through June 30, 2021.
- 5 17 C.F.R. § 230.506(b); see <https://www.sec.gov/smallbusiness/exemptofferings/rule506b>.
- 6 17 C.F.R. § 230.506(c); see <https://www.sec.gov/smallbusiness/exemptofferings/rule506c>.
- 7 17 C.F.R. § 230.504; see <https://www.sec.gov/smallbusiness/exemptofferings/rule504>.
- 8 17 C.F.R. § 227.100 *et seq.*; see <https://www.sec.gov/smallbusiness/exemptofferings/regcrowdfunding>.
- 9 Securities Act of 1933 § 3(a)(11), 17 C.F.R. § 230.147, and 17 C.F.R. § 230.147A; see <https://www.sec.gov/smallbusiness/exemptofferings/intrastateofferings>.
- 10 17 C.F.R. § 230.251 *et seq.*; see <https://www.sec.gov/smallbusiness/exemptofferings/rega>.
- 11 15 U.S.C. § 77a, *et seq.*; see <https://www.sec.gov/smallbusiness/goingpublic>.
- 12 See <https://www.sec.gov/investor/alerts/ipo-investorbulletin.pdf> for more information.
- 13 See <https://twitter.com/adammgrant/status/1418217471488806912>.
- 14 This graphic is based on DERA data. The maps included in this section depict the amounts reported or estimated as raised by issuers, including pooled investment funds that report a primary location in the U.S., including U.S. territories, from July 1, 2020 through June 30, 2021. See *supra* note 3 for a description of how these amounts were reported or estimated.
- 15 This graphic is based on DERA data. This graphic presents capital raised in registered, Regulation D and Regulation A offerings across the top six industries from July 1, 2020 through June 30, 2021. Offerings by non-pooled investment funds in other industries accounted for approximately \$67 billion, \$29 billion and \$40 million in registered, Regulation D and Regulation A offerings, respectively. Regulation A and registered offerings were classified into industry groups based on the primary SIC code

- reported by the company. Industry groups were self-reported by companies on Form D. Differences in data sources and definitions may limit the comparability of industry data. Offerings by pooled investment funds, which accounted for approximately \$183 billion and \$1.7 trillion in registered offerings and Regulation D, respectively, are excluded from this graphic. *See supra* note 3 for a description of how these amounts were reported or estimated.
- 16 This report looks at data from exempt offerings that take place under Regulation Crowdfunding and parallel offerings under Rule 506(c) of Regulation D. *See* Crowdfund Capital Advisors, “How U.S. SME’s Successfully Raised Capital in 2020, Via Online Platforms,” (Feb. 1, 2021) at 21, *available at* <https://crowdfundcapitaladvisors.com/downloads/2020-year-in-review/>.
 - 17 *Id.* at 49.
 - 18 *Id.* at 48.
 - 19 *See* Sherwood Neiss, “Day 1 of #10days10trends,” (July 13, 2021) *available at* <https://twitter.com/woodien/status/1414925426405769221>; *see also* Crowdfund Capital Advisors, *supra* note 16, at 12 (noting that according to a survey of businesses that raised \$1 million using Regulation Crowdfunding, 45.5% had female founders and 40.9% had minority founders).
 - 20 This graphic is based on DERA data. Because of lags in offering qualifications, withdrawals, and abandonments, for greater comparability, this analysis considers all initiated Regulation Crowdfunding offerings and does not exclude offerings that are subsequently withdrawn or abandoned.
 - 21 This graphic is based on DERA data. *See supra* note 3 for a description of the methodology used to calculate this data.
 - 22 This graphic is based on DERA data. This graphic includes all industries that accounted for over five percent of the reported amounts raised by non-pooled fund issuers during one of the respective periods. Offerings by non-pooled fund issuers in other industries accounted for approximately \$45 billion and \$62 billion in the twelve months ended June 30, 2020 and 2021, respectively. *See supra* note 3 for a description of the methodology used to calculate this data.
 - 23 This graphic is based on DERA data. Because of lags in offering qualifications, withdrawals, and abandonments, for greater comparability, this analysis considers all initiated Regulation A offerings (whether qualified or not) and does not exclude offerings that are subsequently withdrawn or abandoned. Due to lags and bunching in proceeds data and temporary relief provided to Regulation A in March 2020, the dollar amounts in this graphic are based on the amounts sought (in \$ million) in qualified Regulation A offerings and not on reported proceeds.
 - 24 This graphic is based on DERA data. This graphic includes all industries that accounted for approximately five percent of the aggregate amounts sought in qualified Regulation A offerings during one of the respective periods. Additional offerings accounted for approximately \$37 million and \$81 million in the twelve months ended June 30, 2020 and 2021, respectively.
 - 25 This graphic is based on DERA data, including pooled funds.
 - 26 This graphic is based on DERA data, excluding pooled funds.
 - 27 This graphic is based on DERA data, excluding IPOs filed by pooled funds. This graphic includes the top six industries by IPO proceeds. Additional offerings by non-pooled fund issuers accounted for approximately \$3.4 billion and \$10 billion in the twelve months ended June 30, 2020 and 2021, respectively. Pooled investment funds, including SPACs, accounted for approximately \$22 billion and \$176 billion in the twelve months ended June 30, 2020 and 2021, respectively.
 - 28 *See* Kyle Stanford, “Alternative Sources of Financing for Startups,” *PitchBook*, (Feb. 11, 2020) at 12, *available at* <https://pitchbook.com/news/reports/q1-2020-pitchbook-analyst-note-alternative-sources-of-financing-for-startups> (noting that VC is not a fit for all businesses or founder personalities). *See also* Thomas Huckabee, “Not All Startups Are a Fit for the VC Funding Model: Why They Need Projected Revenues of over \$25 Million,” *Thomas Huckabee, Inc.*, (June 11, 2021) *available at* <https://tehcpa.net/uncategorized/not-all-startups-are-a-fit-for-the-vc-funding-model-why-they-need-projected-revenues-of-over-25-million/>.
 - 29 *See* Babson College, “Global Entrepreneurship Monitor 2020/2021 United States Report,” (Sept. 3, 2021) at 24, *available at* <https://issuu.com/babsoncollege/docs/gem-2020-2021-us-report>.
 - 30 *See* U.S. Census Bureau, “Business Formation Statistics,” (Oct. 14, 2021) *available at* https://www.census.gov/econ/bfs/pdf/bfs_current.pdf; *see also* McKinsey & Company, “Trends That Will Define 2021 and Beyond: Six Months On,” (July 21, 2021) *available at* <https://www.mckinsey.com/industries/public-and-social-sector/our-insights/trends-that-will-define-2021-and-beyond-six-months-on>.
 - 31 *See* U.S. Small Business Administration Office of Advocacy, “Frequently Asked Questions,” (Nov. 2021) *available at* <https://cdn.advocacy.sba.gov/wp-content/uploads/2021/11/03093005/Small-Business-FAQ-2021.pdf> (calculated using The Census Bureau’s Business Employment Dynamics (BED) data, defining small businesses as independent businesses with fewer than 500 employees).
 - 32 *See* Jessica Looze and Sameeksha Desai, “How Does COVID-19 Affect Challenges Facing Entrepreneurs? Trends by Business Age,” *Ewing*

- Marion Kauffman Foundation, (Dec. 16, 2020) available at <https://www.kauffman.org/entrepreneurship/reports/how-covid-19-affects-challenges-facing-entrepreneurs-by-business-age/> (“Close to half of entrepreneurs with a new business under 1 year old reported information, education, or knowledge necessary for running a business as a challenge (48%). This is more than twice what was reported by those with a mature business (21%).”). See also Jessica Looze and Sameeksha Desai, “Challenges Along the Entrepreneurial Journey: Considerations for Entrepreneurship Supporters,” *Ewing Marion Kauffman Foundation*, (May 2020) at 6, available at <https://www.kauffman.org/wp-content/uploads/2020/05/Challenges-Along-The-Entrepreneurial-Journey.pdf>.
- 33 See Jessica Looze and Sameeksha Desai, “How Does COVID-19 Affect Challenges Facing Entrepreneurs? Trends by Business Age,” *supra* note 32.
- 34 See Start Us Up, “America’s New Business Plan,” (2021) at 16, available at <https://www.startusup-now.org/wp-content/uploads/sites/12/2021/03/AmericasNewBusinessPlan.pdf>.
- 35 See CB Insights, “The Top 12 Reasons Startups Fail,” (2021) at 4, available at https://www.cbinsights.com/reports/CB-Insights_Top-Reasons-Startups-Fail.pdf. (CB insights analyzed 111 startup failures since 2018).
- 36 See Federal Reserve Banks, “2021 Report on Employer Firms. Small Business Credit Survey,” at 7, available at <https://www.fedsmallbusiness.org/medialibrary/FedSmallBusiness/files/2021/2021-sbcs-employer-firms-report>.
- 37 *Id.* at 8.
- 38 *Id.* at 24. Percentages add to more than 100 because respondents could select multiple options. Unlike prior years, the Federal Reserve’s Small Business Credit survey did not include data about the use of retained earnings for ongoing business operations.
- 39 *Id.* at 18 (37% represents a 6% decline from the prior year’s 43% of firms).
- 40 See U.S. Small Business Administration, Office of Advocacy, “Small Business Lending in the United States, 2019,” at 1, available at <https://cdn.advocacy.sba.gov/wp-content/uploads/2020/09/10092858/Report-2019-Small-Business-Lending-Report.pdf>.
- 41 See Office of the Advocate for Small Business Capital Formation, *supra* note 2, at 30.
- 42 See Federal Reserve Banks, *supra* note 36, at 20.
- 43 See Gregory Brown *et al.*, “Filling the U.S. Small Business Funding Gap,” *Frank Hawkins Kenan Institute of Private Enterprise*, (Feb. 2020) at 7, available at http://uncipc.org/wp-content/uploads/2020/02/FundingGap_02042020.pdf; see also <https://proxy.www.sba.gov/loans-grants/get-ready-apply/check-your-credit/collateral#>.
- 44 See Federal Reserve Banks, *supra* note 36, at 17 (large banks included those with at least \$10 billion in total deposits).
- 45 See Jeffrey Sohl, “The Angel Market in 2020: Return of the Seed and Start-Up Stage Market for Angels,” *Center for Venture Research*, (May 5, 2021) at 1, available at https://paulcollege.unh.edu/sites/default/files/resource/files/2020-analysis-report_.pdf.
- 46 *Id.*
- 47 *Id.*
- 48 *Id.* at 2.
- 49 See Angel Capital Association, “Angel Funders Report 2021,” at 8, available at <https://www.angelcapitalassociation.org/angel-funders-report-2021/>.
- 50 *Id.* at 11.
- 51 *Id.* at 5.
- 52 *Id.* at 8.
- 53 *Id.* at 56.
- 54 *Id.* at 12.
- 55 See <https://www.sec.gov/jargon-z#S>.
- 56 See Andy Stinnes, “Seed is Not the New Series A,” *TechCrunch*, (June 21, 2021) available at <https://techcrunch.com/2021/06/21/seed-is-not-the-new-series-a/>.
- 57 See PitchBook-NVCA, “Venture Monitor Q2 2021,” (July 13, 2021) at 7, available at https://nvca.org/wp-content/uploads/2021/07/Q2_2021_PitchBook-NVCA_Venture_Monitor-1.pdf.
- 58 *Id.*
- 59 *Id.* at 8.
- 60 See Alicia Robb, Ph.D., “Rural Entrepreneurship and the Challenges Accessing Financial Capital: An Overview of Funding in Rural America,” (Sept. 10, 2021) at 18, available at https://www.sec.gov/files/2021_Rural_Report_508_Compliance_FINAL.pdf.
- 61 See PitchBook-NVCA, *supra* note 57, at 7.
- 62 See Kyle Stanford, “Angels: Foundational Investors to VC,” *PitchBook*, (Sept. 1, 2020) at 10, available at https://files.pitchbook.com/website/files/pdf/Q3_2020_PitchBook_Analyst_Note_Angels_Foundational_Investors_to_VC.pdf.
- 63 See PitchBook-NVCA, *supra* note 57, at 9. Data from https://sharepoint/sites/oasb/Documents/Annual%20Report/FY2021/External%20Source%20PDFs/Q2_2021_PitchBook_NVCA_Venture_Monitor_Summary_XLS.xlsx?Web=1.
- 64 *Id.* (Excel data).
- 65 See Paul Gompers, *et al.*, “How Venture Capitalists Make Decisions,” *Harvard Business Review*, (Mar.-Apr. 2021) available at <https://hbr.org/2021/03/how-venture-capitalists-make-decisions>.
- 66 *Id.*
- 67 Diversifying Opportunity in Venture Capital: Investing with Emerging Managers (Mar. 31, 2021) available at <https://www.youtube.com/watch?v=318UXLOox3I>.

- 68 See PitchBook-NVCA, *supra* note 57. (Excel data).
- 69 See Paul Gompers *et al.*, *supra* note 65.
- 70 See Peter Walker, “Private Market Report: Q1 2021,” *Carta*, (May 6, 2021) at 8, available at <https://carta.com/blog/private-market-report-q1-2021/>.
- 71 See NVCA, “2021 Yearbook,” (Mar. 2021) at 29, available at <https://nvca.org/wp-content/uploads/2021/03/NVCA-2021-Yearbook.pdf>.
- 72 See Peter Walker, “The State of Private Markets: Q2 2021,” *Carta*, (Aug. 4, 2021) at 9, available at <https://carta.com/blog/private-markets-q2-2021>.
- 73 See PitchBook-NVCA, *supra* note 57. (Excel data).
- 74 *Id.* (Excel data; new and emerging fund managers is defined as those who has sponsored four or fewer funds).
- 75 *Id.*
- 76 See Yuliya Chernova, “A Comeback of First-Time Venture Fund? Stay Tuned,” *Wall Street Journal*, (Sept. 7, 2021) available at <https://www.wsj.com/articles/a-comeback-of-the-first-time-venture-fund-stay-tuned-11631012400>.
- 77 See Marina Temkin, “VC is Performing Better than Ever. Then Why are so Few First-time Funds Being Raised?” *PitchBook*, (May 4, 2021) available at <https://pitchbook.com/news/articles/vc-is-better-than-ever-why-so-few-first-time-funds>; see also PitchBook-NVCA, *supra* note 57, at 26.
- 78 See First Republic, “Fundraising Best Practices for Emerging Managers,” (Apr. 2021) at 5, available at <https://www.firstrepublic.com/-/media/frb/documents/pdfs/innovators/how-to-successfully-raise-a-fund-ii-report.pdf>.
- 79 See PitchBook-NVCA, *supra* note 57, at 19; see also James Thorne, “Corporate VC Firms Buck ‘Tourist’ Reputation with Pandemic Dealmaking,” *PitchBook*, (Sept. 28, 2020) available at <https://pitchbook.com/news/articles/corporate-vc-firms-pandemic-deal-making-rate-bucks-tourist-reputation>; see also James Thorne, “What’s Driving Private Equity’s March on VC?,” *PitchBook*, (Sept. 8, 2021) available at <https://pitchbook.com/news/articles/private-equity-nontraditional-investors-vc-deals>; see also Cameron Stanfill *et al.*, “Crossing Over Into Venture,” *PitchBook*, (Apr. 20, 2021) at 2, available at <https://pitchbook.com/news/reports/q2-2021-pitchbook-analyst-note-crossing-over-into-venture>.
- 80 See Cameron Stanfill *et al.*, *supra* note 79, at 3-5.
- 81 See Cameron Stanfill *et al.*, “Q2 2021 US VC Valuations Report,” (May 2021) at 3-5, available at https://files.pitchbook.com/website/files/pdf/PitchBook_Q2_2021_US_VC_Valuations_Report.pdf (report and Excel packet).
- 82 See Cameron Stanfill *et al.*, *supra* note 79, at 3-5.
- 83 *Id.* at 7.
- 84 See PitchBook-NVCA, *supra* note 57, at 6.
- 85 Data on U.S. listed domestic firms was estimated by DERA based on the Center for Research in Security Prices (CRSP) database. The analysis includes U.S. common stocks (share codes 10 and 11) listed on NYSE, NYSE MKT and Nasdaq. The analysis excludes investment funds and trusts (Standard Industrial Classification codes 6722, 6726, 6798, and 6799). A company with several classes of shares is counted once. Data for 2021 represents the number of listed firms and market capitalization as of September 30, 2021.
- 86 See Joan Farre-Mensa, “Public vs Private Firms,” *WEFI Lecture Series*, (Nov. 2020) at slides 39-40, available at <https://drive.google.com/file/d/1c-GyZ3mMo2IcS7tG8PF16QpnWYSd74WZA/view>.
- 87 See Professor Michael Klausner, United States Securities and Exchange Commission Small Business Capital Formation Advisory Committee, (Sept. 27, 2021) at 136, available at <https://www.sec.gov/info/smallbus/acsec/sbcfac-transcript-092721.pdf>. “And then post-merger, of course, you’re – all of this dilution is drawing a big company and post-merger dilution becomes a smaller fraction”.
- 88 This graphic is based on DERA data for non-SPAC IPOs and SPAC offerings. Data on direct listings are from Jay R. Ritter, Initial Public Offerings: Updated Statistics, October 1, 2021 (the data were pulled from Table 13a) available at <https://site.warrington.ufl.edu/ritter/files/IPO-Statistics.pdf>.
- 89 See Jay R. Ritter, *supra* note 88, at Table 4c, available at <https://site.warrington.ufl.edu/ritter/files/IPO-Statistics.pdf>. This table excludes IPOs with an offer price below \$5.00 per share, unit offers, ADRs, closed-end funds, natural resource limited partnerships, SPACs, REITs, bank and S&L IPOs, small best efforts offerings, offerings by companies that were already traded in other countries, and firms not listed on CRSP within six months of the IPO. CRSP covers stocks listed on Nasdaq, NYSE, and NYSE MKT.
- 90 See Morgan Stanley Institute for Sustainable Investing, “Sustainable Value: How Emerging Public Companies Can Deliver on ESG Expectations,” (2020) at 2, available at https://www.morganstanley.com/content/dam/msdotcom/en/assets/pdfs/3327223_Sustainable-Value-Delivering-ESG-Expectations_FINAL_REVISED.pdf.
- 91 See James Thorne, “Institutional Demand Buys Socially Conscious SPACs,” *PitchBook*, (Feb. 16, 2021) available at <https://pitchbook.com/news/articles/investor-demand-esg-spacs>.
- 92 See Morgan Stanley Institute for Sustainable Investing, *supra* note 90, at 5.
- 93 *Id.* at 3.

- 94 See Renaissance Capital, “Equity in Equities: MWVBE Investment Banks are on the Rise in IPOs,” (Feb. 18, 2021) *available at* <https://www.renaissancecapital.com/IPO-Center/News/77940/Equity-in-equities-MWVBE-investment-banks-are-on-the-rise-in-IPOs>; *see also* Jay R. Ritter, *supra* note 88, at Table 4c. This table excludes IPOs with an offer price below \$5.00 per share, unit offers, ADRs, closed-end funds, natural resource limited partnerships, SPACs, REITs, bank and S&L IPOs, small best efforts offerings, offerings by companies that were already traded in other countries, and firms not listed on CRSP within six months of the IPO. CRSP covers stocks listed on Nasdaq, the NYSE, and the NYSE MKT.
- 95 This graphic is based on DERA data. Registered offering data includes IPOs and registered secondary equity offerings, and was collected from Thomson Financial’s SDC Platinum database. Registered debt offerings have been excluded. Small public companies include public companies with a size less than or equal to \$250 million on the date of the offering, calculated by multiplying price of the company’s stock at the close of the day of the offering by the number of outstanding shares on the day of the offering. Data from the Center for Research in Securities Prices (CRSP), Dealogic, Compustat, and Bloomberg were used to fill in missing information from SDC Platinum. Those companies with missing a stock price on the offering day or number of outstanding shares are not included in the statistics.
- 96 *See supra* note 95 for a description of the methodology used to estimate registered equity offerings by small public companies. This graphic includes all industries that accounted for approximately five percent or more of the total proceeds raised in registered equity offerings by small public companies during one of the respective periods, excluding offerings filed by pooled funds. Additional offerings for industries under five percent accounted for approximately \$0.6 billion and \$1.7 billion in the twelve months ended June 2020 and 2021, respectively. Offerings by pooled funds, including SPACs, accounted for approximately 6 billion and 41 billion in the twelve months ended 2020 and 2021, respectively.
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- 105 *See* U.S. Chamber of Commerce, “Special Report on Women-Owned Small Businesses During COVID-19,” (Aug. 26, 2020) *available at* <https://www.uschamber.com/workforce/special-report-women-owned-small-businesses-during-covid-19>.
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- 110 *See* Jeffrey Sohl, *supra* note 45, at 2.
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- 184 See, e.g., “Women Business Owners and Investors” section of the Report above, at 42-43.
- 185 See, e.g., “Minority Business Owners and Investors” section of the Report above, at 49.
- 186 *Id.* at 48, 51.
- 187 See also North American Securities Administrators Association (NASAA), “Legislative Agenda for the 117th Congress Principle One,” (2019) available at <https://www.nasaa.org/policy/legislative-policy/legislative-priorities/legislative-agenda-for-the-117th-congress-principle-one/> (encouraging proactive education and outreach to underserved and minority entrepreneurs).
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- 190 *Id.* at 21, 25.
- 191 Market participants look at staff guidance when trying to determine whether broker registration is required. See “Notice of Proposed Exemptive Order Granting Conditional Exemption from the Broker Registration Requirements of Section 15(a) of the Securities Exchange Act of 1934

- for Certain Activities of Finders,” Release No. 34-90112; File No. S7-13-20 (Oct. 13, 2020) at 15, available at <https://www.sec.gov/rules/exorders/2020/34-90112.pdf>.
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- 200 See *Report on the 40th Annual Small Business Forum* (Sept. 27, 2021) at 21, available at https://www.sec.gov/files/2021_OASB_Annual_Forum_Report_FINAL_508.pdf.
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- 206 *Id.* at 38; see also Office of the Advocate for Small Business Capital Formation, *supra* note 2, at 43; see also Office of the Advocate for Small Business Capital Formation, Annual Report for Fiscal Year 2019,” at 25, available at https://www.sec.gov/files/2019_OASB_Annual%20Report.pdf.
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OFFICE OF THE
ADVOCATE FOR SMALL
BUSINESS CAPITAL
FORMATION

U.S. Securities and
Exchange Commission
100 F Street NE
Washington, DC 20549
202.551.5407
www.sec.gov/oasb
smallbusiness@sec.gov

