Chairwoman Waters, Ranking Member McHenry, and members of the Financial Services Committee, thank you very much for the opportunity to submit written testimony regarding capital formation and the state of the U.S. IPO market.

By way of background, I am the Managing Partner for Andreessen Horowitz, a $16.5 billion multi-stage venture capital firm focused on IT-related investments. Some of the companies in which we have invested and with which you may be familiar include AirBnB, Coinbase, Github, Roblox, Instagram and Lyft.

I also serve on various investment committees, including for the St. Jude Children’s Cancer Hospital and the Stanford Medical Center, and teach entrepreneurship and venture capital at the Stanford Graduate School of Business. I previously served as the Chairman of the Board of Directors for the National Venture Capital Association, during which time I had the privilege of meeting many of you and your colleagues. Prior to joining Andreessen Horowitz, I held several executive positions in a publicly-traded software company and was previous to that an investment banker.

There are a number of trends concerning IPOs and capital formation to note:

- First, the raw number of IPOs has declined significantly: From 1980-2000, the US averaged roughly 300 IPOs per year; from 2001-2016, the average fell to 108 per year. With the benefit of increasing IPOs in the last few years, we are starting to see better growth: in 2020, there were close to 500 IPOs in the U.S., double the rate of the prior year, 103 of those being venture-backed companies.
- Second, the characteristics of IPO candidates have changed: fewer small companies are making it to the public markets.
  - “Small” IPOs – companies with less than $50m in annual revenue at the time of IPO – have declined from more than 50% of all IPOs in the 1980-2000 timeframe to about 25% of IPOs from 2001-2016;
  - Companies are staying private much longer – the median time to IPO from founding hovered around 6.5 years from 1980-2000; companies are now staying private for 10 or more years from founding;
  - As a result of companies staying private longer, the average size of IPOs has also grown significantly: in 2020, the average IPO raised $353 million, with 18% of all IPOs raising more than $500m each; and
  - Special Purpose Acquisition Vehicles (“SPACS”) represented 50% of all IPOs in 2020, a five-fold increase relative to 2019. In the first quarter of 2021 alone, SPACs raised $87.9 billion, more than was raised in the entirety of 2020, an admittedly banner year for SPACs.
- Third, the cumulative effect of these changes is a hollowing out of the broader US capital markets and a decline in corporate competition: the number of publicly listed companies...
in the US declined by 50% over the last 20 years, while other developed countries have experienced a 50% increase over the same time period.

A number of implications flow from these trends:

• First is jobs. Publicly-traded companies drive employment growth – companies that go public increase employment by 45% relative to private companies. Jobs in competitive industries of course remain key to the goal of sustained and broad economic growth;

• Second is expanding access to economic opportunity: The US needs more public companies creating economic opportunity in areas of the country that are undergoing structural unemployment challenges resulting from a modernizing economy; and

• Third, we are at-risk of creating a two-tiered capital markets structure in the US: one in which the majority of the appreciation accrues to those institutions, pension funds, and wealthy individuals who can invest in the private markets and a second for the vast majority of individual Americans who comprise the retail investor base in the public markets.

- A simple example illustrates this wealth shifting effect from public market investors to private investors. Microsoft went public in 1986 at a $350 million market cap; today, Microsoft’s market cap exceeds $1.8 trillion. Contrast that with Facebook, which debuted in the public markets around a $100 billion market cap. While Facebook has performed well in the public markets, the returns to public market investors are about 8.5x. For public investors in Facebook to achieve returns comparable to those of Microsoft shareholders, Facebook would need to reach a market cap of $500 trillion, a number that well exceeds the total global market cap of all listed stocks.

- While un-accredited Americans do have some access to private markets via the investments that some public mutual funds have made in private companies, the amount of this exposure is very limited. The value of mutual fund investments in private tech companies was estimated at just north of $7 billion in 2016, or about .05% of total US mutual fund assets.

While the reasons for how we arrived at this destination are beyond the scope of this hearing, the trends remain clear.

Before offering some suggestions about how we might improve capital formation, I’d like to review the current state of the IPO market. Despite, the negative trends noted above in terms of overall volume and the later-stage nature of IPOs, the good news is that we have seen areas of innovation and progress in the market over the past few years.

Importantly as well, the positive implications of the 2012 JOBS Act cannot be understated. We have seen improved capital formation as a result of this legislation and the U.S. capital markets remain the deepest and broadest markets for the very best issuers. The combination of access to a robust private market coupled with the easing of the on-ramp created by the JOBS Act has enabled companies such as Moderna to be able to invest in life-changing technologies as we’ve
seen with the recent COVID vaccines. I would be remiss if I didn’t acknowledge the wisdom of Congress in passing this very important legislation.

**Direct Listings:**
Although there has been much talk of direct listing potentially overtaking the traditional IPO, we have seen very few of them in the venture-backed space. To date, only six companies have chosen this path over three years, representing well less than 1% of the total capital markets debuts over the same time period. They have occupied significant attention, however, because 3 of the direct listings are in the top 5 opening trade volumes in the history of the traditional IPO/Direct Listing market.

Given the paucity of direct listings, it is hard to draw too many conclusions from the limited data set. However, below we provide some data on what has been observed to date.

Unlike in an IPO where the banks purchase primary shares directly from the company and resell them to public market investors, in a direct listing there is an opening auction by which the exchanges (New York Stock Exchange (NYSE) or Nasdaq) or their designees (“market makers” in the NYSE case) solicit “bids” (the price and volume at which a buyer wants to transact) and “offers” (the price and volume at which a seller wants to transact). The auction process continues until a sufficient number of orders are “matched” – buyers and sellers are willing to transact at an agreed-upon price and volume to open the stock.

Matching for the completed direct listings vary from a low of 2% to a high of 8% - meaning that percentage of the total shares outstanding have traded in the opening auction. A simple average would get you to around 5%. In contrast, traditional IPOs in the tech space have average around 2% trading volume on the opening trade. This may be one of the reasons why the “IPO Pops” for direct listings are more muted than we have seen recently for more traditional tech IPOs.

For the direct listings completed to date, the stocks have traded in the first day in the range of 15-23% of the total shares outstanding. So, the total first-day volume is about 3-5 times the number of shares that are exchanged in the opening auction. Not all of those shares are additional secondary shares that come into the market. Rather, much of that trading volume reflects the re-trading of shares that were initially exchanged in the opening price auction. We estimate that about one-third of the total shares that trade on opening day of a direct listing are newly-introduced into the market, whereas two-thirds of the trading represents re-trading of those shares.

Traditional IPOs in the tech space have traded closer to 12% of total shares outstanding on the first day of trading – well below what we have seen in direct listings. One explanation for that is, as noted above, direct listings have done a better job of getting initial share volume into the market (~5% on the opening trade vs 2% in traditional IPOs). Second, by better matching supply and demand, direct listings have generally mitigated the magnitude of IPO Pops, thus engendering better overall price discovery.
Most IPOs have lockups that prevent additional secondary shares coming into the market, sometimes for as long as 6-months. Because direct listings generally don’t have lockups (Palantir being the only exception), they enable more secondary shares to be offered to the market post-initial trade, thus reducing price movements caused by supply/demand imbalances in a traditional IPO.

Thus, while the results are still early, we do seem to see better price discovery and reduced after-market volatility from the direct listing process.

**SPACs:**

As noted above, the most significant change in the IPO markets in recent years is the dramatic increase in the number of SPACs raised – constituting 50% of the IPO market in 2020, with the first quarter of 2021 eclipsing the full 2020 number. In April 2021, however, the SPAC new issue volume dropped to 13 deals, a decline of roughly 90% from the March 2021 volume.

There are many theories speculating about the causes of the rapid decline in SPAC issuances, among which are:

- SEC warnings to issuers about potential accounting restatements stemming from option grants issued to promoters;
- SEC warnings to retail investors to be cautious about “celebrity-endorsed” SPAC offerings;
- Overall volatility in the public equity markets and, in particular, contraction in trading multiples for high-growth stocks;
- Delays caused by backlogs and thus longer SEC reviews of de-SPAC offering documents, resulting in existing holders of SPAC shares having less capital to invest in new issuances; and
- Overall poor after-market performance of de-SPAC’d entities.

Proponents of SPACs argue that SPACs offer shorter timelines for companies to become public and with greater certainty of completion (and less pricing risk) than are characteristic of traditional IPOs. As to the former, Nasdaq has published data showing that for the roughly 72 de-SPAC transactions that had been completed as of February 2021, the time to market averaged 4 months versus approximately 6 months for traditional IPOs. The de-SPAC process is essentially the process that occurs after a SPAC has agreed to terms with an acquisition target where the two entities are fully merged.

Performance has been more un-even. According to Nasdaq – again looking at the 72 de-SPAC’d transactions through February 2021 – only 64% have outperformed the S&P 500. Reuters has recently reported that 90% of SPACs that have announced transactions in 2021 are lagging the S&P 500.
A recent study by Professors Michael Klausner and Michael Ohlrogge provides the most comprehensive view to date of the underlying financial behavior of SPAC investors and the after-market performance of SPACs through June 2020.

Among the findings are:

- SPAC dilution amounts to roughly 50% of the cash ultimately delivered to the companies brought public. These costs are much higher than those for IPOs, even accounting for IPO Pops;
- SPAC shares tend to drop by one third of their value or more within a year following a merger, leaving investors who hold shares post de-SPAC most vulnerable to price declines; and
- SPAC investors typically differ from de-SPAC investors. The former are often institutional shareholders who can earn rates of return as high as 11% for “loaning” money to the SPAC in search of its target. However, most SPAC shareholders exit at the time of the de-SPAC, leaving a new set of de-SPAC investors to hold the shares.

Traditional underwritten IPOs:
With the exception of 2020 and the first quarter of 2021, traditional IPOs remain the predominant method of going public.

Much has been written about the concept of what is referred to as the “IPO Pop.” In essence the IPO Pop is the increase in the price of the opening trade of an IPO relative to the IPO price. Concerns have been raised around what this reveals about the price discovery process for IPOs and whether retail investors are disadvantaged relative to certain institutional investors that have access to purchase shares at the IPO process.

We have published some research on this topic elsewhere, which I will summarize briefly below.

First, as the below chart shows, IPO pops are not a new phenomenon. In fact, if you exclude the Dot Com Bubble of 1999-2000, they have been steady for nearly thirty years.

<table>
<thead>
<tr>
<th>Time Period</th>
<th>IPO Pop*</th>
</tr>
</thead>
<tbody>
<tr>
<td>1980-1989</td>
<td>6.1%</td>
</tr>
<tr>
<td>1990-1998</td>
<td>13.3%</td>
</tr>
<tr>
<td>1999-2000</td>
<td>51.6%</td>
</tr>
<tr>
<td>2001-2019</td>
<td>13.7%</td>
</tr>
</tbody>
</table>

[*IPO Pop = mean increase in stock price from IPO price to 1st-day close. Source: [https://site.warrington.ufl.edu/ritter/files/IPOs2019_Underpricing.pdf](https://site.warrington.ufl.edu/ritter/files/IPOs2019_Underpricing.pdf)*]

Second, the size of the IPO Pop is mostly a function of the demand for a given stock. Gauging demand for an IPO can be difficult, but a rough proxy for the relative magnitude of the
institutional demand is whether a company’s final offering price is above, within or below its initial filing range (IFR).

<table>
<thead>
<tr>
<th>Time Period</th>
<th>% Below IFR</th>
<th>% Within IFR</th>
<th>% Above IFR</th>
</tr>
</thead>
<tbody>
<tr>
<td>1980-1989</td>
<td>30%</td>
<td>52%</td>
<td>13%</td>
</tr>
<tr>
<td>1990-1998</td>
<td>27%</td>
<td>49%</td>
<td>24%</td>
</tr>
<tr>
<td>1999-2000</td>
<td>18%</td>
<td>38%</td>
<td>44%</td>
</tr>
<tr>
<td>2001-2019</td>
<td>33%</td>
<td>45%</td>
<td>22%</td>
</tr>
</tbody>
</table>

[Source: https://site.warrington.ufl.edu/ritter/files/IPOs2019_Underpricing.pdf]

When we combine the data from the two charts, we can discern some conclusions.

<table>
<thead>
<tr>
<th>Time Period</th>
<th>IPO Pop</th>
<th>% Above IFR</th>
</tr>
</thead>
<tbody>
<tr>
<td>1999-2000</td>
<td>51.6%</td>
<td>44%</td>
</tr>
<tr>
<td>2001-2019</td>
<td>13.7%</td>
<td>22%</td>
</tr>
<tr>
<td>1990-1998</td>
<td>13.3%</td>
<td>24%</td>
</tr>
<tr>
<td>1980-1989</td>
<td>6.1%</td>
<td>13%</td>
</tr>
</tbody>
</table>

[Source: https://site.warrington.ufl.edu/ritter/files/IPOs2019_Underpricing.pdf]

Interestingly, the proxy for demand – the percentage of IPOs that priced above the initial filing range – seems directionally correlated with the size of the IPO pop. If you plot the individual years between 1990-2019, you see a fairly strong correlation (r-square = 58%) between percentage of IPOs pricing above the high end of the file range and the average first-day return.

What appears to be happening is that bankers increase the final offering price relative to the initial filing range more frequently when they assess greater institutional demand during the roadshow, and, at the same time, the buyside likely gets lower than their desired allocations in a “hot” IPO. The combination of these two factors would create stronger after-market performance as the marginal buyers increase their ownership (and as the momentum investors chase the price performance); thus, a higher IPO pop.
Third, the supply of IPO shares being offered by the company, otherwise referred to as the float (the quotient of the number of shares sales in the offering divided by the total shares outstanding for the company) has changed over time.

The below chart shows median % IPO floats over various time periods: median floats were pretty consistent from 1980-1998, but fell significantly during the Dot Com Bubble,

<table>
<thead>
<tr>
<th>Time Period</th>
<th>Median % IPO Float</th>
</tr>
</thead>
<tbody>
<tr>
<td>1980-1989</td>
<td>40%</td>
</tr>
<tr>
<td>1990-1998</td>
<td>45%</td>
</tr>
<tr>
<td>1999-2000</td>
<td>25%</td>
</tr>
</tbody>
</table>


And how does this change in floats manifest itself in the magnitude of IPO Pops?

<table>
<thead>
<tr>
<th>Time Period</th>
<th>Low Float IPO Pop</th>
<th>High Float IPO Pop</th>
</tr>
</thead>
<tbody>
<tr>
<td>1980-1989</td>
<td>1.8%</td>
<td>1.9%</td>
</tr>
<tr>
<td>1990-1998</td>
<td>10%</td>
<td>6.3%</td>
</tr>
<tr>
<td>1999-2000</td>
<td>37.5%</td>
<td>9.9%</td>
</tr>
</tbody>
</table>


With the exception of the 1980-1989 time period (where we know that IPO pops overall where the lowest), the size of the IPO pop is correlated with the float: lower floats (meaning that there are fewer shares available to trade, aka low supply) yield higher first-day pops.

As noted above, the demand side of the equation – whether IPOs are priced above their initial filing range – also influences the size of the IPO float. The below charts illustrates that interplay between supply (float) and demand (pricing above the initial filing range).

<table>
<thead>
<tr>
<th>Time Period</th>
<th>Low Float % of Companies Pricing Above the Range</th>
<th>High Float % of Companies Pricing Above the Range</th>
</tr>
</thead>
<tbody>
<tr>
<td>1980-1989</td>
<td>14%</td>
<td>11%</td>
</tr>
<tr>
<td>1990-1998</td>
<td>28%</td>
<td>18%</td>
</tr>
<tr>
<td>1999-2000</td>
<td>48%</td>
<td>30%</td>
</tr>
</tbody>
</table>


In 2020, we have seen even smaller floats. At approximately 15%, the median float is well below historical norms; not surprisingly, this is one reason why we see much higher IPO Pops in recent IPOs relative to historical norms. Constrained supply drives the after-market prices higher.
And why are floats so much lower? One likely contributor is the fact that venture-backed
companies in particular are staying private much longer (nearly double the 6-7 year time frame
that we saw through the early 2000’s). As a result, they are much more mature at the time of IPO
(median revenue is about 10x what is what in the Dot Com bubble) and thus much higher valued.
So, even assuming they wanted to raise the same amount of nominal dollars at the IPO as in the
past, a higher valuation means they can do so by issuing many fewer shares.

How can we improve the overall state of the IPO markets, economic growth and retail access to
capital?

As has been noted, the good news for capital formation is that there are now multiple choices for
companies that are considering going public: traditional IPOs, direct listings and SPACs. We
hope this competition among listing options can drive down costs and reduce friction in the
public offering process, thus encouraging more companies into the public markets. In fact, we
are already seeing some positive improvements in the market as a result of competition.

For example, lockups agreements, which distort short-term trading in the markets by artificially
reducing the amount of tradeable float, are starting to be modified to enable more staged
“dribbles” of stock at various time frames and price points versus the all-or-nothing 6-month
lockups that have existed for most traditional IPOs. In addition, some underwriters are enhancing
their price discovery mechanisms for traditional IPOs to reduce IPO Pops and dampen first-day
trading volatility.

However, even with this competition, we still face a situation where too few companies go
public and, when they do so, they go public at much later stages of maturation. As a result, job
growth attendant with public companies is impacted and retail investors’ access to high-growth
stock appreciation is limited.

There are, however, a number of things that legislators and regulators could consider that would
help ensure flexibility while achieving the economic growth and retail investor access goals.

Opportunities to make it easier for issuers to become public companies (and at earlier stages of
maturity):

Expand Emerging Growth Company (EGC) Status - One of the most successful
aspects of the Jumpstart our Business Startups (JOBS) Act was the creation of the EGC
designation for growth companies accessing the public markets. EGC designation
smooths the transition to the public markets for innovative growth companies, making an
IPO relatively more attractive.

Two improvements to the eligibility criteria for EGCs would create greater certainty
around regulatory status for companies considering whether to go public:
• Extend the timeframe for EGC eligibility from five years to ten years for certain exemptions and disclosure requirements. Existing legislation, the *Helping Startups Continue to Grow Act* sponsored by Representative Bryan Steil (R-IN), would make these improvements for small capitalization companies.

• Provide a transition period of one year for EGCs who trigger large accelerated filer status when their public float exceeds $700 million for the first time.

**Require Short Position Disclosure** - A short position disclosure regime similar to that which exists for material long positions would support innovative small-capitalization companies by requiring that investors disclose material short positions they hold. There currently exists an information vacuum which encourages certain investors to promote misleading information and inaccurate data that can drive a company’s stock price down while hiding the true source and financial interest behind those efforts. Small capitalization companies are particularly vulnerable to these so-called “short and distort” campaigns as they often have shallow liquidity and limited research coverage, meaning their share price can move quickly based upon investor sentiment.

**Allow EGCs to choose trading venues** - With the proliferation of new trading venues that have been created over the last twenty years, fragmentation of shares trading across venues has become an increasing challenge for smaller companies with less liquidity. Fragmentation leaves smaller companies more vulnerable to short-term volatility that can further erode liquidity and dry up research coverage. Providing EGCs the opportunity to opt out of unlisted trading privileges (UTP) and select the venues that can trade their securities will improve trading volume for these companies and improve capital formation in the public markets.

**Review regulatory barriers to research coverage for EGCs** - A lack of consistent research coverage has become one of the most significant disincentives for smaller companies trying to decide whether to become publicly listed. Research coverage for small-capitalization companies in particular has dropped dramatically. Research coverage is particularly important for companies with thinly traded stocks, as name recognition is often low, trading can be volatile, and the universe of investor interest is limited. Engaging a study to examine ways that policy can reduce the barriers to research coverage for EGCs would be helpful to improving overall liquidity.

**Review potential barriers to diversified mutual fund ownership of EGCs** – Diversified mutual funds are typically restricted to owning no more than 10% of the float of publicly-listed companies. Given that mutual funds have grown significantly in size, they often find it difficult to acquire meaningful positions in smaller-cap companies owing to these concentration limits. To encourage greater institutional participation, Congress and the SEC should consider, potentially for a limited period of time relative to a new issue, increasing the concentration limits for diversified mutual funds. Allowing mutual funds to hold slightly larger positions in newly issued stocks would increase the
economic incentives for them – material appreciation in a stock could have a meaningful impact on the overall fund performance.

Opportunities to encourage issuer choice of paths by which to come public to engender fair competition, enhanced price discovery and broader retail participation:

Clarify the tracing rules with respect to direct listings – Because direct listings to date have been largely completed with secondary shares, Section 11 liability for selling shareholders for potential misstatements in the offering documents remains unclear. The “tracing” rules in a traditional IPO typically require that a plaintiff be able to trace the share purchased in the after-market to the registration statement for those shares. In a direct listing, many shares are typically sold under Rule 144 and thus not registered until a traditional offering document (only the shares outside of 144 are typically registered). Because of this uncertainty around potential liability for selling shareholders (including in pending litigation underway currently), direct listings may not achieve their full potential. Clarification around the liability regime would be helpful to clear-up the current tracing rule ambiguity.

Ensure appropriate disclosures and liability regimes around SPACs – Currently, in connection with the de-SPAC process, many SPACs provide 5-year forward forecasts that are used in connection with the marketing process for the pending acquisition. Some have argued that the Private Securities Litigation Reform Act (PSLRA) safe harbor applies to such disclosures, in effect providing a shield against private securities actions for sponsors in connection with the de-SPAC process. The SEC’s Director of the Division of Corporate Finance recently provided some guidance raising questions about the extent of PSLRA coverage. However, clear guidance from Congress or the SEC about this would go a long way to ensuring that traditional IPOs are not disadvantaged relative to SPACs in a competitive marketplace. In addition, clarity on this topic would ensure that retail investors (who are typically different from the institutional investors who purchase the initial SPAC shares and often exit the company pre de-SPAC) are provided with all material information around the acquisition and with appropriate legal protections for any material misstatements.

In addition, Congress and the SEC should consider conducting further studies on the issues highlighted by the research of Professors Klausner and Ohlrogge to better understand the trading dynamics of SPACs, the redemption behavior of institutional investors and the ultimate dilution borne by shareholders post de-SPAC. Such an inquiry could lead to enhanced disclosures to retail investors in particular about the nature of the shareholder base they may be joining in connection with the de-SPAC.

Congress and the SEC should also consider conducting further studies on the “promote” economics in SPAC transactions and consider whether additional disclosure is required to ensure that all investors understand potential conflicts that may arise between sponsors
and non-sponsor shareholders. In some cases, promotes may be “shared” with PIPE investors, which could meaningfully impact the return opportunities for sponsors and PIPE investors relative to retail investors who buy shares in the open market.

It is worth noting that, even in the absence of new regulatory guidance, the SPAC markets are already “self-correcting” in response to institutional investor feedback. For example, PIPE investors are increasingly requiring that sponsor’s remain holders of their shares for longer periods of time post de-SPAC, and the size and nature of sponsor promotes are also being impacted.

Ensure appropriate SEC resources to increase the throughput of public offerings – Given the increased options for companies to go public, we have heard that the SEC staff has been overwhelmed by the volume of offerings in its review pipeline. As a result, turnaround times for companies to be declared effective and thus access the public markets have become longer and less predictable. When timing risks are uncertain, on balance, companies may pursue other avenues (e.g., acquisitions) or may chose the shortest possible go-public path, independent of the relative merits of other options. To ensure maximum flexibility for issuers, Congress should consider whether the SEC has adequate resources to manage a growing pipeline of companies seeking to go public.

Opportunities to enhance access to private markets for non-institutional investors

As noted above, as companies stay private for longer periods of time, more of the appreciation opportunities inherent in high-growth companies is reserved for institutional investors and wealthy individuals who have access to private market investments. Thus, while looking for ways to make it easier for companies to go public earlier is important, we should also look to ways to expand access to retail investors in the private markets. Importantly, however, we should not lose sight of investor suitability and overall investor protections, even as we seek to expand broader retail access.

Amend the Accredited Investor definition to expand its ranks – The SEC has taken an initial step toward this by creating effectively a “knowledge” safe harbor to include more individuals in the definition, but Congress and the SEC should look at ways to materially increase the number of individuals who would qualify under a revised definition. One shorthand for this may be to incorporate the Crowdfunding rules mechanism, which provides for absolute dollar amounts that may be invested by individuals regardless of accredited investor status. To ensure investor protection, any amendments to the rules could be restricted to private funds that would provide investors the benefits of diversification and professional fund management (vs providing a broad exemption for individual company investments).

Amend the 3(c)(1) restrictions on the number of Accredited Investors for private funds – Most private funds today are limited under Rule 3(c)(1) to accepting no more
than 100 accredited investors. As a result, nearly all of the capital raised by these funds comes from qualified clients or qualified institutional purchasers. In addition to expanding access to the accredited investor definition, Congress and the SEC should consider whether to amend the 100-person limit to enable broader individual access to private funds. In addition, to ensure investor protection, consider amending the rules to create a dollar limit (versus a number of persons limit). For example, one could limit accredited investors to no more than 10-20% of a total fund’s assets under management to ensure that there is also strong institutional support behind the private fund manager.

**Amend the RIA restrictions on incentive-based compensation** – Under current rules, registered investment advisers (RIAs) are prohibited from charging incentive-based fees for accredited investors. As a result, access to private funds for these investors are limited. Coupled with the regulatory changes noted above and with appropriate disclosures, Congress and the SEC should consider amending these rules to permit incentive-based compensation as a way to increase accredited investor access to private funds.

**Enhance access to private investments via mutual funds** – Today, closed-end funds are limited to holding no more than 15% of their total assets in private offerings, unless they restrict fund access to accredited investors only. Models, such as those proposed by Representative Anthony Gonzalez (R-OH) in the *Increasing Investors Opportunities Act*, which would eliminate this limitation, could also enhance retail access to private, high-growth opportunities.

**Enhance access to private, secondary market transactions** – Today, un-accredited individual investors are permitted under the Crowdfunding rules to invest in early-stage seed companies, but are prohibited from investing in later-stage, pre-IPO companies. This makes little sense when you consider the differential risks of loss associated with those two very different stages of investments. To expand retail access to private market opportunities, Congress and the SEC should consider amending these rules to permit access to later-stage, pre-IPO companies. This of course needs to be accompanied by enhanced regulatory disclosures, but supporting venues who seek to enter this business opportunity through reformed regulation would expand access to high-growth opportunities.

**Opportunities to enhance access to capital formation and individual participation in investment opportunities via effective blockchain regulation.**

We believe that blockchain holds the promise to be the next transformative industry, provided the policy environment allows entrepreneurs to fully experiment with the technology in the U.S. The current discussions around blockchain have many similarities to the regulatory policy conversations that occurred during the rise of previous generations of new industries, such as biotechnology and the commercialization of the Internet. In each of these cases, doubts amongst
policymakers proliferated and policy proposals were considered that could have prevented American leadership before the full promise of the technology was realized. Fortunately, cooler heads prevailed, and as a result, the U.S. has been the unquestioned global leader in technological innovation since World War II.

The commercialization of blockchain technology is in its infancy, but a glimpse into the current efforts of blockchain entrepreneurs offers a clear illustration of its potential. As we speak, blockchain entrepreneurs are working to apply the technology to solve critical societal challenges like access to financial services for the unbanked and underbanked, expanding economic opportunity, fighting climate change, and providing a market-based solution to technology and financial services industry concentration. These individuals are undertaking the risky endeavor of entrepreneurship to explore how the power of open protocols can fundamentally redesign how individuals and businesses use the internet.

The benefit of blockchain development is that the ultimate users and community members associated with the various projects can receive tokens during the infancy of a project as a reward for their participation. This democratization of access to tokens means that, if the projects are ultimately successful and thus the value of the token accretes alongside the utility value derived from the project, these market participants can benefit from that appreciation. Thus, in many ways, a healthy blockchain ecosystem not only creates economic growth and technological developments in the U.S., but it also is an opportunity for anyone who desires to be part of a project to also benefit from the success of that endeavor.

Unfortunately, the SEC has not provided clear regulatory guidelines for how tokens will be treated under existing regulatory rules. Rather, the SEC has focused predominantly on bringing enforcement actions against bad actors. While this is laudable, it has failed to provide clarity for the many determined good actors who seek to develop blockchain projects that are both successful and regulatorily compliant. This inability to differentiate between good faith technology entrepreneurs and get-rich-quick schemes makes the SEC’s job of policing this activity even harder.

To ensure U.S. leadership in this very important area of technology development, Congress and the SEC should create an effective blockchain regulatory regime. The bipartisan Token Taxonomy Act provides a base of work for policymakers to do so. In addition, the Eliminate Barriers to Innovation Act of 2021 is also constructive in this regard. Establishing a clear regulatory framework for blockchain technology is a difficult task, as with any emerging technology field, but it is a priority shared by many policymakers on both sides of the aisle and most industry participants. We urge policymakers to do what previous generations of regulators were able to accomplish when faced with similar challenges in innovative technologies: construct a regulatory regime that allows the technology to develop in a safe and sustainable manner.
I thank you for your time and for the opportunity to discuss the very important topic of capital formation in the U.S. As I think we all recognize, ensuring that the U.S. continue to create new jobs that result from new company formation is critical not only to our economic future, but also to our national security and sovereignty.

While I have tried to offer a number of suggestions to achieve this outcome, these are by no means exhaustive. I look forward to the opportunity to work with the Committee to the extent it determines to continue its work in this area.