Speech

Remarks to the Small Business Capital Formation Advisory Committee

Commissioner Mark T. Uyeda

Washington D.C.

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Good morning and welcome to the first meeting of 2024. First, congratulations to Stacey Bowers for becoming the new Advocate for Small Business Capital Formation. I look forward to working with Stacey in her new role. The two topics on the committee's agenda for today – the accredited investor definition and declining number of initial public offerings ("IPOs"), especially among smaller companies – are important issues for capital formation.

I have had nearly 29 years of experience with Regulation D and the accredited investor definition – as a securities lawyer in private practice, as a state securities regulator, and at the Commission. We have discussed this topic at prior meetings[1] and last month, I focused my remarks at a securities law conference on this topic.[2] I raised the question whether we should move away from an "all or nothing" approach, where an accredited investor can invest 100% of his or her assets in a single private offering, but if you are a dollar short of qualifying as an accredited investor, you cannot invest at all. Should we allow an individual to invest up to certain percentages of a personal financial metric, like the aggregate dollar value of his or her securities investments, in private offerings? For example, if a person's securities investments were less than $100,000, then the person could invest up to 5% of such amount in private offerings over a rolling 12-month period. If securities investments were between $100,000 and $500,000, then the person could invest a higher percentage. When the person's securities investments exceed a certain level, that limitation could be removed.

As the committee deliberates the accredited investor definition, I encourage consideration of the following three themes:

1. Do Not be Restricted by the Past. Some have called for the net worth and annual income thresholds to be indexed to inflation from the levels established in 1982, but this assumes that these levels were correct to begin with. Moreover, it assumes that net worth and annual income are the appropriate metrics for assessing an individual's ability to invest in private offerings. Formulate your recommendations from a blank canvas and do not be tied by decisions made over forty years ago.
2. Opportunity, not Paternalism. Any regulatory approach to private offerings should focus on opportunity rather than paternalism. The ability of more individuals to participate in private offerings should be viewed as a benefit, not a detriment. A paternalistic approach, with the government

deciding who can and cannot invest, may ultimately harm the exact persons who it is trying to protect. The harms include depriving individuals from accumulating wealth, reducing opportunities for risk diversification, and furthering economic inequality. This harm may have a disproportionate impact on Black and Hispanic investors,[3] younger investors, and investors in rural areas. Reducing opportunities to invest in private offerings may make it more difficult for entrepreneurs to obtain early-stage financing. Remember to consider the opportunities lost with a paternalistic approach.

3. Not a Tool to Prevent Private Companies from Failing or Committing Fraud. Many start-up companies fail because their business model does not produce the intended results. Other companies fail because of fraud and mismanagement. However, failed business models and fraud are not limited to private companies and often occur at public companies – look at the many enforcement actions brought by the Commission. Yet, the Commission's rules do not limit investments in public companies to only investors who meet certain wealth or income thresholds. And investors have their own tools to protect themselves from the risks of private investments: they can diversify and, more importantly, if an issuer will not provide information requested by the investor, they can walk away. Develop your recommendations knowing that these other tools exist.

Our economy can have vibrant private and public markets at the same time, and our regulatory regime should aim for that result. Thus, the second topic on the agenda today – the decline of IPOs, especially among smaller companies – is also important. According to the most recent annual report prepared by the Commission staff, smaller companies have accounted for the "vast majority" of the decline in exchange-listed companies in the last 25 years.[4] Furthermore, acquisitions of smaller public companies account for a significant portion of that decline.[5] Why are smaller companies leaving the public markets at a greater rate than larger companies? Are relatively higher compliance costs and relatively lower research coverage[6] among the reasons? If so, how can the Commission's rules reverse this trend? I look forward to hearing your findings and recommendations.

Thank you, and I hope that you have a productive meeting.

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[1] *See*, *e.g.*, Mark T. Uyeda, Remarks to the Small Business Capital Formation Advisory Committee (Sept. 19, 2023), available at https://www.sec.gov/news/speech/uyeda-remarks-sbcfac-091923 and Mark T. Uyeda, Remarks to the Small Business Capital Formation Advisory Committee (June 14, 2023), available at https://www.sec.gov/news/speech/uyeda-remarks-sbcfac-061423.

[2] Mark T. Uyeda, Remarks at the 51st Annual Securities Regulation Institute (Jan. 22, 2024), available at https://www.sec.gov/news/speech/uyeda-remarks-securities-regulation-institute-012224.

[3] Office of the Advocate for Small Business Capital Formation, Annual Report Fiscal Year 2023, at p.73, available at https://www.sec.gov/files/2023-oasb-annual-report.pdf.

[4] Id. at p.33.

[5] *Id*.

[6] *Id*. at p.38.