September 10, 2019

Hon. Maxine Waters
Chairwoman
Committee on Financial Services
U.S. House of Representatives
Washington, D.C. 20515

Hon. Patrick McHenry
Ranking Member
Committee on Financial Services
U.S. House of Representatives
Washington, D.C. 20515

Hon. Carolyn Maloney
Chairwoman
Subcommittee on Investor Protection,
Entrepreneurship, and Capital Markets
Committee on Financial Services
U.S. House of Representatives
Washington, D.C. 20515

Hon. Bill Huizenga
Ranking Member
Subcommittee on Investor Protection,
Entrepreneurship, and Capital Markets
Committee on Financial Services
U.S. House of Representatives
Washington, D.C. 20515

Re: Hearing on Examining Private Market Exemptions as a Barrier to IPOs and Retail Investment

Dear Chairwomen Waters and Maloney, Ranking Members McHenry and Huizenga, and Members of the Committee:

Thank you for your ongoing efforts to promote robust capital markets. The Healthy Markets Association[1] appreciates the opportunity to offer our thoughts on this important hearing, "Examining Private Market Exemptions as a Barrier to IPOs and Retail Investment."

We hope this hearing will mark a turning point for the Committee. Congress and the SEC have pushed trillions of dollars in capital out of the well-regulated, public markets and

[1] The Healthy Markets Association is an investor-focused not-for-profit coalition working to educate market participants and promote data-driven reforms to market structure challenges. Our members, who range from a few billion to hundreds of billions of dollars in assets under management, have come together behind one basic principle: Informed investors and policymakers are essential for healthy capital markets. To learn more about Healthy Markets, please see our website at http://www.healthymarkets.org.

into the far-less-regulated "private" markets,[2] which has had profound impacts on investors, workers, companies, and the overall economy.

Spurred by years of deregulation by Congress and the SEC, the number and volume of "private" offerings has grown dramatically, from once just a fraction of the overall markets to now more than 60%. At the same time, there are now fewer than half the number of public companies as there were in the mid-1990s.

Now that so many companies are operating without basic public disclosures and so much capital is being raised outside of the federal regulatory regime, some are suggesting you and the SEC should deregulate even further so as to "ease access" to growth-stage companies. For example, some have proposed expanding the tradability of "private" securities or expanding the pool of potential investors in "private" securities to include even less sophisticated or wealthy investors.

These proposals would not spur any new capital formation. Nor would they help investors. The federal securities laws promote -- not inhibit -- the efficient allocation of capital within our economy because they ensure that market participants have the information they need about companies to properly assess those companies' values. Further, the federal securities laws ensure that all investors have the same access to essential information about their investments. It levels the playing field. Expanding the scope, number, and breadth of offerings outside of these laws takes away information needed to make efficient decisions and puts investors on a field that is often tilted against them. Those who are most vulnerable will be harmed the most.

Not surprisingly, when compared to private securities, public securities typically offer a number of significant advantages for investors, including:

- Public securities typically are accompanied by more robust accounting and business disclosure practices.
- Information about public companies, including third party research, is much more readily available and fairly distributed (as required by SEC rules).
- Public securities are far more easily and reliably valued.

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[2] For the purposes of this comment, "private" offerings are those made in reliance on an exemption or exception to the general registration requirement of the Securities Act of 1933. Further, we refer to "private" companies as those that have not made a registered offering and are not subject to the ongoing reporting obligations or other elements of the Securities Exchange Act of 1934 ("Exchange Act"). Were colloquially refer to "public" companies as those that have engaged in a registered offering or are otherwise subjected to the ongoing reporting and other obligations of the Exchange Act.

- Public securities offer a transparent and efficient method to liquidate shares of common stock.
- Liquidity risks and trading costs for public securities are often significantly lower than for similarly-situated private securities.
- Public securities are much more easily benchmarked, such as against the S&P 500; and
- Actual net performance tends to be at least as good, if not better, for institutional investors (and is markedly better for less sophisticated investors).

While the framing of this hearing suggests a welcome recognition that the proliferation of private offering exemptions has harmed the public markets, most of the legislative proposals included for discussion do not. A number of them would further expand the private markets at the expense of the public markets. Importantly, there is no credible evidence to support the assertion that any of the deregulatory proposals before the Subcommittee at this hearing would individually or collectively increase the number or dollars raised by IPOs, promote job creation, or improve capital allocation in the broader economy.

Instead of promoting efficient allocations of capital, several of the bills before the Subcommittee, as well as the proposals outlined by the SEC's recent Concept Release,[3] will divert companies and capital out of the public markets on the one hand, while also deteriorating the number and quality of public offerings on the other. We urge you to go in the opposite direction and consider proposals to collect greater information about the private markets, and engage in multi-faceted efforts to promote the public markets.

Background on the Federal Securities Laws and the Rise of Private Markets

In the aftermath of the Great Crash, Congress adopted the Securities Act of 1933 to require the registration of public offerings of securities. The goal was to make sure that people buying a security had key information about the company, its financials, and its governance so that they could properly value it, and thus ensure the efficient allocation of capital to drive not just a company, but the entire economy forward.[4]

[3] *Concept Release on Harmonization of Securities Offerings*, SEC, Sec. Act Rel. No. 33-10649, Jun. 18, 2019, *available at* https://www.sec.gov/rules/concept/2019/33-10649.pdf.
[4] H.R. Rep. 73-85 (1933).

The Securities Exchange Act of 1934 complements the Securities Act by requiring sufficiently large, widely-held, public companies to meet ongoing reporting obligations, comply with certain governance standards, and more.

The federal securities laws ensure that all investors are given equal access to key information about a public company -- both at the time of a public offering and thereafter. It thus levels the playing field between issuers and investors, as well as between different investors. For example, it is illegal for an executive to selectively disclose information to selected research analysts or investors, but not others,[5] a point the SEC has recently reiterated through an enforcement action.[6]

Beginning in the late 1970s, but really taking steam in the 1980s (with the adoption of Regulation D),[7] Congress and the SEC began to dramatically expand the size of exemptions from the securities laws. These now include Rule 506 offerings, Rule 504 offerings, Rule 144A offerings, Crowdfunding, Reg A offerings, and more. Some of these offering methods had, prior to the adoption of the JOBS Act of 2012, already swamped the general registration requirement, so that the majority of new capital raised by companies was done using these exemptions. The JOBS Act made that even easier, as now a company can raise an unlimited sum from an unlimited number of investors via a SuperBowl halftime commercial and call it a "private" offering.

Further, while the securities laws also were intended to require disclosures of key information from and basic shareholder rights for large, widely held companies, those provisions have also been eroded. For example, at the time Facebook made its IPO, it was already held by thousands of shareholders and had billions of dollars in revenues.[8] Facebook was considered a rarity at the time. Today, there are nearly 500 so-called "unicorns" – companies that attain valuations of $1 billion or more in private markets – including 21 with valuations of more than $10 billion.[9]

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[5] 17 C.F.R. § 243.100, et seq.

[6] *See, e.g., In the Matter of TherapeuticsMD, Inc.*, SEC, Exch. Act Rel. No. 86708 (Aug. 20, 2019), *available at* https://www.sec.gov/litigation/admin/2019/34-86708.pdf.

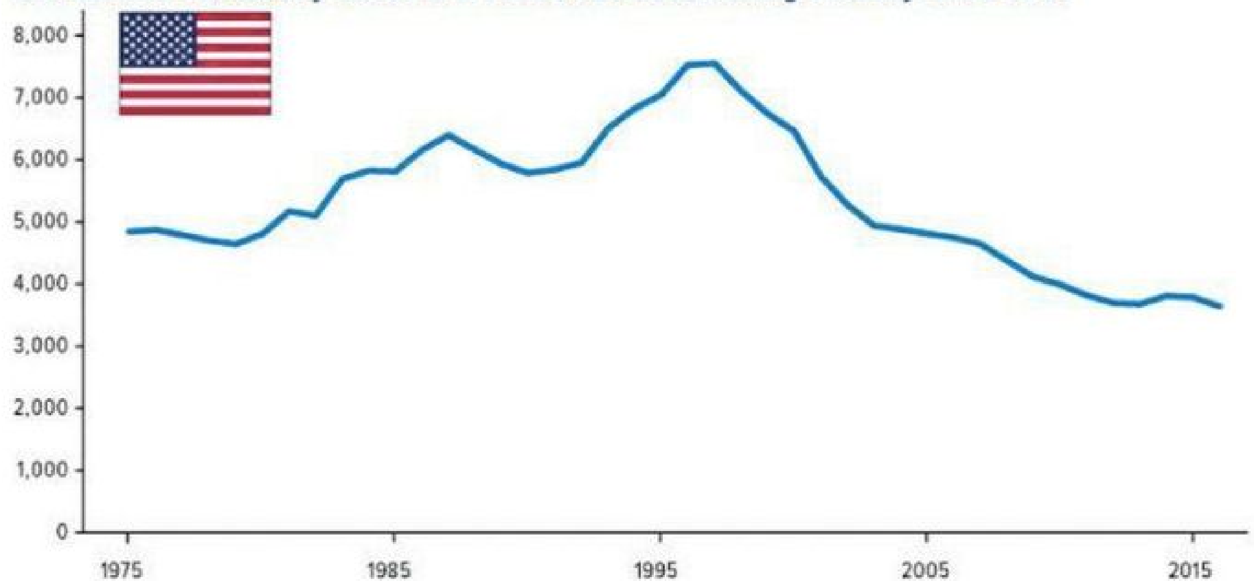
[7] *Revision of Certain Exemptions From Registration for Transactions Involving Limited Offers and Sales*, SEC, 47 Fed. Reg. 11251 (Mar. 16, 1982).

[8] Steven Davidoff Solomon, *Facebook May Be Forced to Go Public Amid Market Gloom*, N.Y. Times, Nov. 29, 2011, *available at* https://dealbook.nytimes.com/2011/11/29/facebook-may-be-forced-to-go-public-amid-market-gloom/ (explaining that "Facebook will almost certainly have to go public during this time whether it wants to or not — and whether or not it can get a valuation of $100 billion or more in doing so. And it's partly Facebook's fault — it just has too many shareholders.").

[9] CrunchBase Unicorn Leaderboards, TechCrunch, *available at* https://techcrunch.com/unicorn-leaderboard/ (viewed Sept. 6, 2019).

Put simply, companies are generally no longer required by law to make basic disclosures and give shareholders basic rights in order to raise the capital they need to survive and grow. So they don't.[10]

Facebook's CEO made the point very clearly nearly a decade ago "If you don't need that capital [from an IPO], then all the pressures are different, and the motivations [to go public] are not there in the same way."[11] Since then, private capital raising has surged, and the number of public companies has continued its steady decline.[12]



[10] Elisabeth de Fontenay, *The Deregulation of Private Capital and the Decline of the Public Company*, 68 Hastings L. J. 445 (2017), *available at* https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2951158.
[11] Jessica E. Vascellaro, *Facebook CEO in No Rush to "Friend" Wall Street,* Wall St. J., Mar. 4, 2010, available at https://www.wsj.com/articles/SB10001424052748703787304575075942803630712 (quoting Mark Zuckerberg).
[12] Frank Holmes, *The Pool Of Publicly Traded Stocks Is Shrinking. Here's What Investors Can Do*, Forbes, August 13, 2018, *available at* https://www.forbes.com/sites/greatspeculations/2018/08/13/the-pool-of-publicly-traded-stocks-is-shrinking-heres-what-investors-can-do/#5b814b0b2078.

In fact, de-listings have outpaced IPOs for most of the past decade.[13] At the same time, companies -- both foreign and domestic -- that are looking to sell securities to American investors are continuing to forgo the public markets as simply unnecessary for their capital raising purposes.[14]

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Where have all the public companies gone?

- Market indexes are experiencing record highs, but there are fewer listed companies today than in 1976; in fact, U.S. listings dropped 50 percent from 1996 to 2016.
- Private companies can now raise late-stage venture and other private capital on equal or better terms than in the public markets — and with less hassle.
- It has become essentially impossible for investors to get diversified exposure to the U.S. economy, and to real economic value creation, without tapping private equity.

COMMENTARY

Caroline Rasmussen, vice president at iCapital Network

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Impact of the Rise of Private Markets

We must begin our discussion of the private markets by acknowledging how little we actually know about them. The SEC doesn't capture complete information about private offerings or private companies. Nor do state regulators. For example, even in its recent

[13] We note that the two primary causes appear to be the rise of private capital raising and mergers and acquisitions activity by often-already public companies. In the case of M&A activity, instead of having multiple public companies, you have one. There are certainly concerns to be raised by these circumstances, such as antitrust considerations, but we understand those to be largely outside the scope of this hearing.

[14] For example, in April 2019, Saudi Aramco sold more than $12 billion in debt using a Rule 144A after postponing an IPO. Interactive Brokers, *Saudi Aramco's Debut Debt Sale Sees Slick Demand*, Seeking Alpha, Apr. 10, 2019, *available at* https://seekingalpha.com/article/4253787-saudi-aramcos-debut-debt-sale-sees-slick-demand; see also, Abhishek Kumar, *Saudi Aramco IPO: Loss For Equities, Gain for Fixed Income?*, State Street Global Advisers, Sept. 5, 2018, *available at* https://www.ssga.com/blog/2018/09/saudi-aramco-ipo.htm.

Concept Release, the SEC merely "estimates" the amounts raised, even though the amounts raised run into the trillions of dollars.

Table 2: Overview of amounts raised in the exempt market in 2018

Exemption	Amounts Reported or Estimated as Raised in 2018
Rule 506(b) of Regulation D	$1,500 billion
Rule 506(c) of Regulation D	$211 billion
Regulation A: Tier 1	$0.061 billion[39]
Regulation A: Tier 2	$0.675 billion[40]
Rule 504 of Regulation D	$2 billion
Regulation Crowdfunding; Section 4(a)(6)	$0.055 billion
Other exempt offerings[41]	$1,200 billion

[15]

Neither the SEC nor state regulators typically know to whom private offerings are made, who buys them, how much is sold, or what information and rights are provided. Nor do they often know of any key changes to the company, its financials, governance, or ownership over time, muchless how that information may or may not be shared or utilized by insiders, investors, or others over time.

But aside from the government itself, the investors in private offerings often do not have the same type and quality of information about the companies, their financials, or their executives that would be required as part of the registration and ongoing reporting processes for public companies.

Perhaps the best way to illuminate the importance of the public markets is to put it into context of other issues that I know this Committee has been examining.

- Just a few months ago, this Subcommittee held a hearing to explore the importance of so-called ESG factors.[16] All of those factors -- ranging from environmental concerns to human capital management to international tax practices -- typically apply to companies in the public markets only.[17]

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[15] Concept Release, at 19.

[16] *Building a Sustainable and Competitive Economy: An Examination of Proposals to Improve Environmental, Social and Governance Disclosures*, Hearing before the Committee on Financial Services Subcommittee on Investor Protection, Entrepreneurship and Capital Markets, 116 Cong. (2019), webcast and written statements available at https://financialservices.house.gov/calendar/eventsingle.aspx?EventID=404000.

[17] Id., (Testimony of James Andrus, CalPERS, at 3)("This raises an important point for today's discussion: most of the ESG-related policy dialogue focuses only on the public markets. Moving forward, we encourage you to also consider how important ESG issues like those we are discussing today can be carried into the non-public market space as well.").

- Similarly, we understand that this Committee has spent significant time studying the proxy process and related disclosures. That process generally applies to companies that are in the public markets only.

- We understand that some members of this Committee are concerned that the SEC may permit companies in the public markets to adopt mandatory investor arbitration provisions. While investors' legal recourse rights haven't generally been limited in public markets, the private markets freely permit such limitations on investor rights' to access the courts.

- We know this Committee has been working on legislation to enhance transparency into actions brought by the Public Company Accounting Oversight Board, the primary regulator of auditors that was created following the Enron and Worldcom frauds. Again, these reforms would benefit investors in the public markets only.[18]

But there are countless more benefits to transparency. For example, if a company subject to Exchange Act obligations engages in wrongdoing, it has to tell the public what it did. There may otherwise be no other way for US regulators or investors to learn of wrongdoing by the company. There is no similar obligation for private companies.

We find it telling what happens when companies do decide to emerge from the private markets and expose themselves to the transparency required by the public markets. As an initial matter, as companies begin the process, a myriad of problems are often identified. These may include significant concerns regarding the company's financial condition and prospects, governance,[19] compliance, operations, and more. The public spotlight, shareholder scrutiny, and legal liabilities that are imposed by the public markets improve efficiency and overall corporate accountability.[20]

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[18] According to its website, the Public Company Accounting Oversight Board "*oversees the audits of public companies* and SEC-registered brokers and dealers in order to protect investors and further the public interest in the preparation of informative, accurate, and independent audit reports." PCAOB, *Mission, Vision, and Values*, *available at* https://pcaobus.org/About/History/Pages/mission-vision-values.aspx (visited Sept. 6, 2019) (emphasis added).

[19] *See, e.g.*, Suhauna Hussain, *Facing backlash, WeWork adds one woman to its all-male board*, L.A. Times, Sept. 4, 2019, *available at* https://www.latimes.com/business/story/2019-09-04/wework-frances-frei-board-ipo (noting pressure from investors to add a woman to the previously all-male board of directors of WeWork in advance of its planned IPO).

[20] For example, after initially receiving criticism once it became public that "WeWork's parent company, The We Company, had paid its CEO [$5.9 million] so the company could acquire the "We" trademark from

Valuations often vary significantly. Perhaps the best, most-recent example of this is Uber Technologies, which made its IPO in May of this year. Just months before making its offering, but before full information was provided, press reports suggested the company could be valued as high as $120 billion.[21] By this time, of course, the company had engaged in numerous rounds of "private" fundraising raising billions of dollars from a large number of investors. Yet, once more complete information was released to the markets pursuant to its S-1 filings and various other communications, the company was valued at $82 billion at the time of its IPO. As of September 6th, still less than three months after its IPO, the company was trading at a market capitalization of under $55 billion.

The company hasn't lost more than half of its users or revenues in this short period or otherwise suffered a catastrophic setback. Rather, market participants were simply given more information about the company. That information allowed them to better analyze the company, its prospects, and ultimately its value. That's precisely what the public capital markets are intended to do--provide more (and more accurate) information to everyone so they can properly assess the value and allocate resources efficiently to drive our economy forward. If Congress misallocated $65 billion it would be a very, very big deal. We're talking about the potential misallocation of $65 billion -- for just one company.

There are also significant concerns with who has access to what information when. In the public markets, companies provide certain required information about their operations, finances, and governance on a regular basis (e.g., quarterly and annual reports), but also whenever anything particularly significant happens. These reports give rise to much more widely available research reports and analysis, which as this Subcommittee has heard many times over the years, is essential for spurring investment.

However, the lack of regular and significant disclosures by companies in the private markets often stifles third-party investment research, as there is generally no way to

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WE Holdings LLC, where Neumann is a managing member," the CEO returned the money to the company. Ann Schmidt, *Adam Neumann returns $5.9M to WeWork after it paid the CEO for 'We' trademark*, Fox Business, Sept. 5, 2019, *available at* https://www.foxbusiness.com/business-leaders/wework-ceo-adam-neumann-returns-trademark-money (citing the company's amended S-1 filing).

[21] Trefis Team, *How Uber Could Justify A $120 Billion Valuation*, Forbes, Dec. 3, 2018, *available at* https://www.forbes.com/sites/greatspeculations/2018/12/03/how-uber-could-justify-a-120-billion-valuation/#76b4aaf97f9b.

access information. It can also severely impair the quality of the research that is available because that research may be based on limited or skewed information. For example, why would a company share bad news when it isn't obligated to do so?

In "private" securities, issuers and investors often negotiate the information and rights for the investors both at the time of the offering and thereafter. And there are typically no requirements that information be widely disseminated.[22] A private company may make selective disclosures that benefit certain investors at the expense of others without likely violating federal or state securities laws--unlike if the company were "public."[23] This lack of consistent information and treatment of investors raises significant concerns of fairness and efficiency for investors and the markets. It should also be noted that this type of discrimination is likely to disproportionately negatively impact smaller, less connected players, such as smaller institutions or so-called "retail" investors.

From an investor's perspective, trading private securities is also much, much riskier and costlier. First, an investor may not even be able to sell a private security. Second, even if an investor can trade, the price at which the investor can trade generally isn't widely available. Compared to public securities, private securities are much more difficult to value. That's because there is much less information available about them, and that information may be selectively disclosed. The investor may have to go back to the investment bank who helped broker the deal or the company itself in order to be given a suggested price. Investors often do not know potential contra-sides of their trades, putting them at distinct disadvantages for negotiating on prices.

But there's also commissions. A broker trading a public stock may make $0.005/share on a trade, but might arrange for a private sale of a similar private security for a fee that is orders of magnitude greater. This is just a transaction cost that doesn't go to either the issuer or the investor--so it does not benefit capital formation or investor returns, but instead goes to the intermediaries.

Most pensions and other conservative institutional investors have self-imposed limits on how much they can invest in these markets because of the much, much greater costs and risks. At the same time, many of these investors are also deeply concerned about

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[22] While the antifraud provisions of federal and state securities laws may provide some protections, these protections may be remarkably limited based on the timing of disclosures, content, and reliance. Put simply, investors' seeking to recover for losses or regulators seeking to pursue an action arising from a false statement made on a S-1 filing are subject to a fundamentally different legal standard than if they are seeking to enforce their rights relying on traditional fraud statutes.
[23] *See, e.g., In the Matter of TherapeuticsMD, Inc.*

missing out on the increasing number of quality investment opportunities that are now in the private markets. So, while many of these investors are concerned with the risks, pressured to chase investment opportunities, many of them are increasing their allocations to private market investments and simply absorbing the greater risks and costs.[24] That said, there is growing research to suggest that even sophisticated institutional investors may not outperform in the private markets versus public markets.[25]

Importantly, as Congress recognized in 1933, the need for consistent information about companies is important not just for investors, but to ensure the proper allocation of capital across our economy. It is only with information that investors can properly value securities, and only with that proper valuation, can the capitalist system work. In 1933, the House Report to what became the Securities Act explained "[w]hatever may be the full catalogue of the forces that brought to pass the present depression, not least among these has been this wanton misdirection of the capital resources of the Nation."[26]

Recent experiences with peeling back information requirements haven't always worked very well. For example, the JOBS Act created, and the SEC has now implemented, so-called Regulation A+, which is essentially an exemption that allows for the public offering and trading of securities with far-lower disclosure obligations than are generally required for registered public offerings. Over one hundred companies have made made filings to suggest that they were going to make such an offering. While the majority of Regulation A+ offerings are not sufficiently publicly traded to allow for tracking of their performance, those that have been listed on NYSE and Nasdaq have been atrocious.[27] As Barron's reported:

> Investment returns are hard to find, mainly because only a few dozen of the 300-odd Reg A+ stocks have gotten so far as to list on the NYSE, NASDAQ, or OTC markets, where you can trade or at least get a price quote. Those include a handful of community banks and one outfit carried high on the recent blockchain froth. Excepting those, the average

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[24] Arlene Jacobius, *CalPERS not alone on private equity shift*, Pensions & Investments, Apr. 1, 2019, *available at* https://www.pionline.com/article/20190401/PRINT/190409988/calpers-not-alone-on-private-equity-shift.

[25] *See, e.g.*, Robert S. Harris, Tim Jenkinson and Steven N. Kaplan, *How Do Private Equity Investments Perform Compared to Public Equity?*, 14 J. Inv. Mgmt. 14, 15 (2016), *available at* https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2597259 (finding that, post-2005, returns were about equal between private and public markets investments by institutional investors).

[26] H.R. Rep. 73-85, at 2-3, (1933).

[27] Bill Alpert, Brett Arends, and Ben Walsh, *Most Mini-IPOs Fail the Market Test*, Barron's, Feb. 13, 2018, *available at* https://www.barrons.com/articles/most-mini-ipos-fail-the-market-test-1518526753.

> Reg A+ stock fell 40% in the six months after its mini-IPO and has underperformed the raging bull market surrounding them by nearly 50 percentage points.[28]

Worse, the one blockchain-related outlier referenced above that performed well has subsequently had its assets frozen in an emergency fraud enforcement lawsuit by the SEC -- just months after its mini-IPO.[29]

The lack of consistent, essential public information about private securities also has profound implications for systemic risk. It's worth remembering that the Great Depression was started when lightly regulated securities were offered and sold to investors without sufficient key information--much like private securities today. Even the most sophisticated investors proved ill-equipped to protect themselves, muchless the broader economy from the collapse.

But far more recently, many of the financial products underpinning the financial crisis (e.g., collateralized debt obligations), were often sold as private offerings that lacked key information.[30] Unsurprisingly, following that crisis, several experts called for the elimination or reduction of some exemptions from the federal securities laws, such as Rule 144A.[31]

Currently, two key investment areas come to mind: leveraged loans and Bitcoin-related financial products. Leveraged loans are often sold as "private" securities. Like the commercial mortgage backed securities of 2007, the details are often not universally known at the time of offering, nor are there necessarily requirements to provide the same information and rights to investors after the initial offering. Nevertheless, many experts and policymakers are already beginning to question whether these products

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[28] Id.

[29] Complaint, *SEC v. Longfin Corp. et. al.*, 18 Civ. 2977, Apr. 4, 2018 (S.D.N.Y.), *available at* https://www.sec.gov/litigation/complaints/2018/comp-pr2018-61.pdf.

[30] See *Wall Street and the Financial Crisis: Anatomy of a Financial Collapse*, Majority and Minority Staff Report of the Permanent Subcmte on Investigations, Senate Cmte on Homeland Sec. and Gov't Affairs, 112 Cong. (2011), *available at* https://www.hsgac.senate.gov/imo/media/doc/PSI%20REPORT%20-%20Wall%20Street%20&%20the%20Financial%20Crisis-Anatomy%20of%20a%20Financial%20Collapse%20(FINAL%205-10-11).pdf.

[31] *See, e.g.*, Jeff Madrick and Stephen Diamond, *A "Modest Proposal" for Capital Market Reform: Close Down Rule 144A*, HuffingtonPost, (May 25, 2011), *available at* https://www.huffpost.com/entry/a-modest-proposal-for-cap_b_564989?guccounter=1&guce_referrer=aHR0cHM6Ly93d3cuZ29vZ2xlLmNvbS8&guce_referrer_sig=AQAAAMAHB5GFI5wQoB3PCBE-c6j8dzrrR5da90U19J3Mrh3OSymyxsgkmNEuWv3998bR3LbTdAZ0_xLxli6qGVzhIEENPmMTG30s7xQCTQgAvX7upHALYO52bg4WyMGLHMBmyvix9za-iJUd1Emj2Pd4MXwk-WHMTnsBiGl7TfyYxuvI.

may be giving rise to significant risks.[32] In this Committee, the Subcommittee on Consumer Protection and Financial Institutions held a hearing on this topic in June.[33]

We pose this question: if these products were sold with the same types of disclosures that accompany registered offerings, would they be giving rise to the same risks? Put another way, if all of the relevant details are adequately disclosed, would investors still be willing to purchase them in the same amounts, or on the same general terms?

The situation regarding Bitcoin products raises even more questions. The SEC has repeatedly rejected requests to permit Bitcoin ETFs, and the staff has articulated several concerns with the products, including how the ETF is valued and how the markets could be manipulated.[34] An asset management firm that has been attempting to have a Bitcoin ETF product approved for several years recently announced that -- without responding to any of the SEC's articulated concerns -- it plans to start selling the product anyways as a "private" offering to institutional investors.[35] Is this good for our markets or investors?

Lastly, we wish to return to where we started: the impact of the exemptions and exceptions on the public capital markets. As we have said before, the number of public companies has steadily declined. Now, more recently, the quality of the companies that are going public has also declined. There was a time when investors would compete for IPO allocations. Now, those circumstances are increasingly rare. But it's not very hard to see why.

According to a recent study by Goldman Sachs, of all the IPOs since 2010, the median newly-public stock performance lagged behind the broad Russell 3000 index by 28

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[32] *See, e.g.*, Jesse Hamilton, *Leveraged-Loan Peril Demands Action by Mnuchin, Key Senator Says*, Bloomberg, Apr. 11, 2019, *available at* https://www.bloomberg.com/news/articles/2019-04-11/key-senate-democrat-urges-mnuchin-to-step-up-on-leveraged-loans.

[33] *Emerging Threats to Stability: Considering the Systemic Risk of Leveraged Lending*, Hearing before the House Financial Services Cmte, Subcmte on Consumer Protection and Financial Institutions, 116 Cong. (2019), *available at* https://financialservices.house.gov/calendar/eventsingle.aspx?EventID=403827.

[34] Letter from Dalia Blass, SEC, to Paul Schott Stevens, ICI, and Timothy Cameron, SIFMA Asset Mgmt Group, Jan. 18, 2018, *available at* https://www.sec.gov/divisions/investment/noaction/2018/cryptocurrency-011818.htm.

[35] Paul Vigna, *Van Eck, SolidX to Offer Limited Version of Bitcoin Exchange-Traded Fund*, Wall St. J., Sept. 3, 2019, *available at* https://www.wsj.com/articles/van-eck-solidx-to-offer-limited-version-of-bitcoin-exchange-traded-fund-11567503003.

percentage points in its first three years of trading.[36] There may be many reasons for underperformance once companies are public. But if we look directly at these companies, we can see that the IPO markets seem to be increasingly companies that

- are not-yet-profitable or particularly close to profitability,[37]
- appear to be exits by key executives or early investors, or
- have relatively extreme risk/reward profiles (such as biotechnology companies in clinical trials).

Companies that are simply looking to raise capital for growth are generally not accessing the public markets. We hope that will change. If the US capital markets are to remain the best in the world, and a driver of our economy in the decades ahead, it must.

What Can Congress Do to Enhance the Public Markets?

We urge you to remember that the role of the public markets is to ensure companies that offer securities to the public, or that are large and widely held, provide sufficient information to allow for accurate valuations, and the efficient allocation of capital to drive our economy.

We recommend taking a four-pronged approach. First, we urge you pause the creation and expansion of exemptions and exceptions from the federal securities laws. Not only do we urge you to stop pursuing legislation that would expand the tradability of private securities or increase the pool of potential investors in private securities, but we also encourage you to stop the SEC from continuing down this path as well.

Second, we urge you to take efforts to ensure the public and regulators have more information about private offerings and private companies. We understand there are some discussion drafts of legislation along these lines before the Subcommittee today, and urge you to consider them. One easy way to ensure market participants and regulators have some of this basic information would be to require significantly more information from those who wish to avail themselves of the existing exemptions. In addition, the SEC should conduct a comprehensive review of each exemption and how it is used, by whom, and the extent to which it is undermining investors and the public markets.

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[36] Chris Mathews, *Investors beware: The typical IPO stock is a dud, says Goldman Sachs*, MarketWatch, Sept. 5, 2019, *available at* https://www.marketwatch.com/story/investors-beware-the-typical-ipo-stock-is-a-dud-says-goldman-sachs-2019-09-05.

[37] Christ Mathews (noting that "only 47% of the IPOs studied achieved profitability by their third year.").

Third, we urge you to consider curtailing or eliminating some of the obvious failures of past efforts to spur capital formation. For example, since its creation in the JOBS Act, Regulation A+ has been a disaster for investors. NYSE has become so concerned with the poor quality of these securities that it has stopped accepting them for listing. Nasdaq is also pulling back. Congress should too.

Fourth, we urge you to consider curtailing the existing exemptions and seek to pull the huge new swath of massive, widely held "private" companies into the light of the SEC disclosure regime. One approach, which was previously offered by Senator Jack Reed (D-RI) as an amendment to the JOBS Act, would be to revise Section 12(g) in a way that would require more widely-held companies to meet ongoing reporting and other requirements.

Conclusion

Thank you for the opportunity to offer our insights into today's hearing. Please feel free to have your staff contact me with any questions or follow up at (202) 909-6138 or by email at ty@healthymarkets.org.

Sincerely,

Tyler Gellasch
Executive Director