ANGEL CAPITAL ASSOCIATION

July 15, 2021

The Honorable Gary Gensler, Chair
Commissioner Hester M. Pierce
Commissioner Elad L. Roisman
Commissioner Allison Herren Lee
Commissioner Caroline A. Crenshaw
Securities and Exchange Commission
100 F Street N.E.
Washington, DC 20549-1090

Dear Commissioners:

On behalf of the Angel Capital Association ("ACA"), the 14,000 accredited angel investors we represent, and the thousands of innovative entrepreneurs we support, we would like to provide historical insights and recent data on the importance of retaining the current definition of Accredited Investor as found in Rule 501((a), Rule 215, and Rule 144A of the Securities Act. We are offering these comments in light of recent statements by Commission members as well as the periodic review of the Accredited Investor definition required under the Dodd-Frank Act.

<u>What is Angel Investing</u>

The Angel Capital Association is the world's largest professional organization of accredited angel investors, who invest individually or through angel groups, accredited on-line platforms and family offices. The Association's members invest <u>their own after-tax money</u> in high growth, early-stage, entrepreneurial companies. There are business angels and angel groups in every state. Last year angel investors wrote an estimated $24 billion in personal checks to 65,000 new companies, creating more than 270,000 new jobs, and supplying as much as 90% of the equity funding for these cutting-edge firms. Companies such as Home Depot, Google, Starbucks, Twitter, and PayPal were initially supported by Angels who believed in the entrepreneurs who founded these firms and helped them thrive.

Angel supported companies are usually too risky to qualify for bank loans and too small or too early for venture capitalists (VCs). In fact, angels invest in 15 times more start-up companies each year than do VC firms. And we provide not just capital, but time, expertise, mentorship, and governance—often to first time entrepreneurs who dearly need this help.

More importantly, Federal census data shows that high growth startups create *all* net new jobs in our country. A widely regarded study from the Census Bureau and Ewing Marion Kauffman Foundation found that since 2008 new businesses account for nearly all net new job growth and close to 20% of gross job creation. The report also found that over the past three decades, companies less than five-years-old have created on average 1.5 million jobs annually.

High-growth early-stage startups are fundamental to our economy. They are the firms that are addressing seminal concerns such as climate change, new vaccines, clean energy, and artificial intelligence, to name a few examples. In addition to enhancing America's competitive standing globally, angel investing improves access to capital for underserved and underrepresented portions of our society, including women, people of color, and rural communities.

Importance of Retaining the Accredited Investor Definition

The Dodd-Frank Act requires the SEC to review the definition of accredited investor every four years. The current definition sets a threshold that is based on wealth requirements and financial sophistication. Currently an accredited investor must have $1 million in net worth (not counting their primary residence) or $200K annual income. Retaining this net worth threshold allows underrepresented individuals and communities to participate in this asset class, particularly those outside of major metropolitan areas, at higher rates than would otherwise be possible if the threshold is increased.

A study conducted by the Angel Capital Association several years ago found that increasing the thresholds to a higher level, such as $2.5 million in net worth, would effectively exclude an estimated 60% of Americans eligible to qualify as "accredited investors." Eliminating 60% of the estimated $24 billion in annual angel investments could amount to a decline of capital flow on the order of $14.4 billion annually.

This would lead to two very negative impacts. First is a very significant capital gap for our job- and innovation-creating founders who are so fundamental to our economy. Increasingly, corporate R&D priorities are shifting away from basic science and innovation, and the economics of venture capital favor larger funds focused on later stage opportunities, leaving angels with the primary responsibility for funding young companies. A reduction in the number of accredited investors would directly reduce the number of angel investors available to fund this incredibly important part of our economy.

Second, not only would this severely curtail available funding to the start-up community, but it would also disproportionately impact women, minorities, and those living in the middle of the country, from qualifying as investors and participating in start-up investments. This diminishment of diversity in the investor ranks would have a direct impact on the diversity of founders backed by early investors. A lack of diversity amongst investors is a frequently cited factor in the relative shortage of funds going to underrepresented founders. Two recent reports are attached which document the adverse impact changing the definition would have on the very populations that President Biden's Administration wants to bring into the mainstream. Given the priority the SEC currently places on this issue, I am sure the Chair and Commissioners will agree that this would be an unacceptable outcome.

The SEC has also expanded the definition of who is considered accredited by allowing investors to become accredited by demonstrating appropriate levels of financial sophistication. The ACA believes this action will improve participation by minorities, women, and younger investors who otherwise are excluded from becoming accredited investors. Our organization has made significant strides in building out a competency to determine investor sophistication and we look forward to working with the SEC in setting curricula that will meet the rigorous requirements of financial sophistication. Together we believe this effort will allow greater participation in the start-up economy as well as help entrepreneurs-of-color and female-led firms to gain wider access to capital while concurrently maintaining necessary investor protections.

Angel Investor Protections are Adequate

We believe that the current accredited investor definition provides adequate protections for mom-and-pop investors and retirees. First, it is important to remember that angels are investing their own after-tax dollars, and are doing so directly. Angels and angel funds do not use brokers or third-party intermediaries to make their investment decisions. The rigor of the due-diligence process followed by angel investors and the groups to which they belong, allows us to become intimately familiar with the extremely early stage companies we are investing in and the entrepreneurs who are leading these start-ups. Further driving the need for direct connection is the significant level of mentorship, coaching and advice these young companies require from angels. Investor fraud in angel investing has been exceptionally low because of this approach. We are often at the front lines of mentoring these start-up entrepreneurs and hold Board seats that allow us to keep a close eye on the performance and financial

management of their companies. In this mentoring capacity, our members donate 1 million hours of volunteer time annually and we have challenged them to double this rate in the years ahead.

Second, our Association, and organizations like ACA, provide in-depth education and training to help accredited investors understand the risks of this asset class. We strongly encourage that newly accredited investors join a seasoned group of fellow investors and participate in ACA University or similar educational options to learn the "dos and don'ts" of being an angel investor. Also, the ACA regularly publishes data and insights on how to better improve investment outcomes, allowing both seasoned and new angels to become better informed about angel investing. Each year, as more data becomes available, additional insights are identified that bring out more of the science behind the asset class.

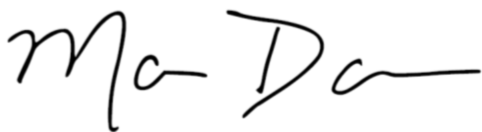
Third, our Association and most other angel entities strongly advise potential investors to make angel investments a small part of their investment portfolio. To characterize us as investing our entire retirement savings that we depend upon to survive is mis-leading and does not represent the profile of the angel investor we have represented for more than 15 years.

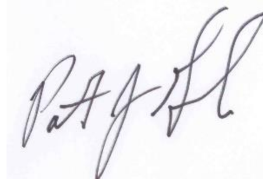
Conclusion

In summary, we are recommending that the Commission follow the adage "If it ain't broke, don't fix it." The existing Accredited Investor definition has met the test of time, has served the entrepreneurial community well, and has been the engine fueling the growth and job creation of this country for many years. We are on the cusp of an opportunity to include more underserved and underrepresented people, particularly women and people-of-color, both within this asset class and as budding entrepreneurs, by retaining the current standards. Narrowing the "goal post" by changing the definition, will only impede access and inclusion to these populations.

The Angel Capital Association stands ready to answer any questions you might have regarding the above information. We also look forward to working with the SEC staff in developing rigorous requirements and qualification procedures to allow professional sophistication to become an avenue for meeting the accredited investor definition. Thank you for considering the information we have provided.

Sincerely,





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Enclosures (2)

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