



ANGEL CAPITAL ASSOCIATION

Angel Investors, Innovative Startups and the Accredited Investor Definition

SEC Advisory Committee on Small and Emerging
Companies

December 17, 2014

Marianne Hudson – ACA Executive Director and Member, Women’s Capital
Connection and Mid-America Angels



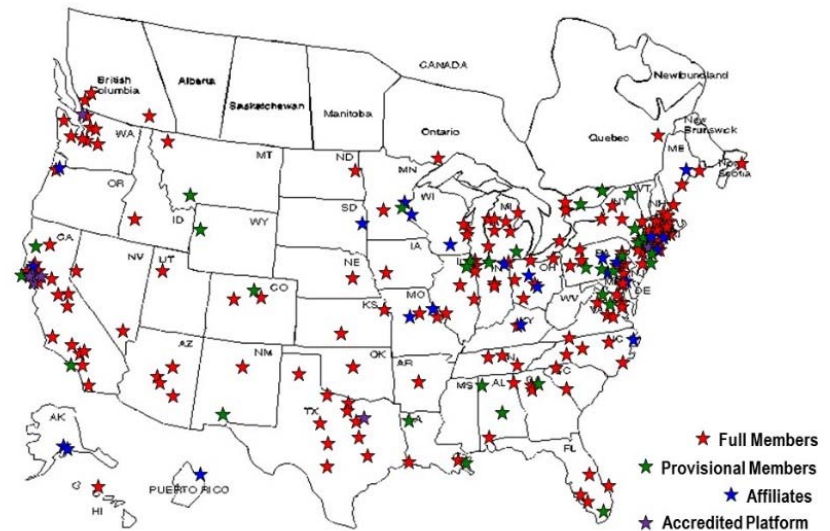
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Angel Capital Association

World's Largest Association of Accredited Angel Investors

www.angelcapitalassociation.org

- 12,000+ individual accredited investors
- 220+ angel groups and accredited platforms
- Voice of accredited angels
 - Best practices
 - Public policy



Mission: fuel success of angel groups and accredited investors and the early-stage companies they support

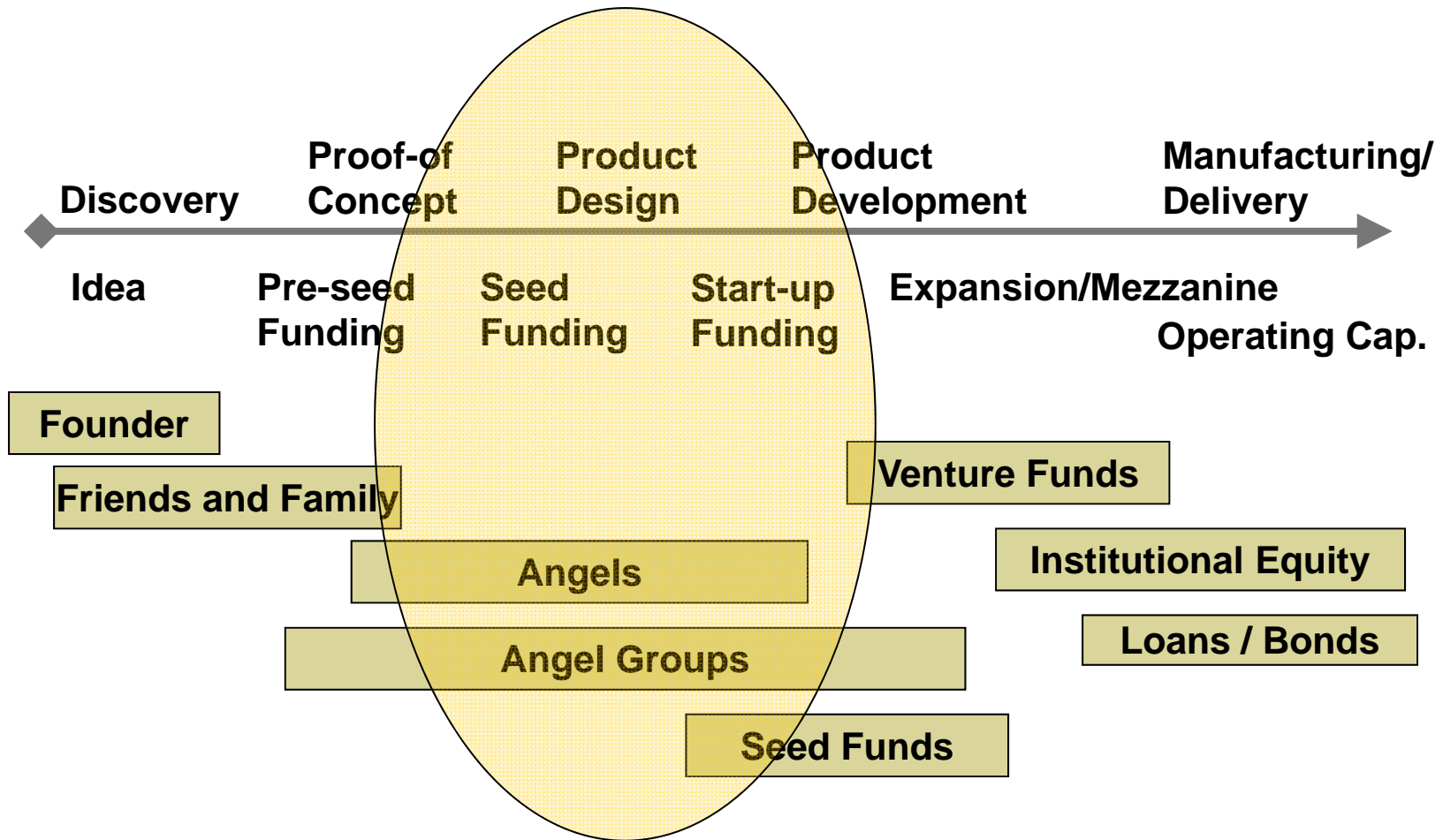


Accredited Investor Definition Recommendations

1. Leave the financial thresholds where they currently are
 - Clearly understood and worked well for decades
 - Increases for inflation would have large market impact and reduce capital pool for entrepreneurs
 2. Add sophistication criteria to grow the base for individuals who do not meet the thresholds
 - Ensure measures are simple to administer
 - Provide multiple criteria to ensure many qualify
 3. Make investor education more widely known and available
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Financing Life Cycle





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Angels Provide Less Equity by Total Dollars – BUT...

- Angel Investors (\$25B)
- Venture Capital (\$30B)
- Private Equity (\$347B)





Angels Drive Most Startup Funding

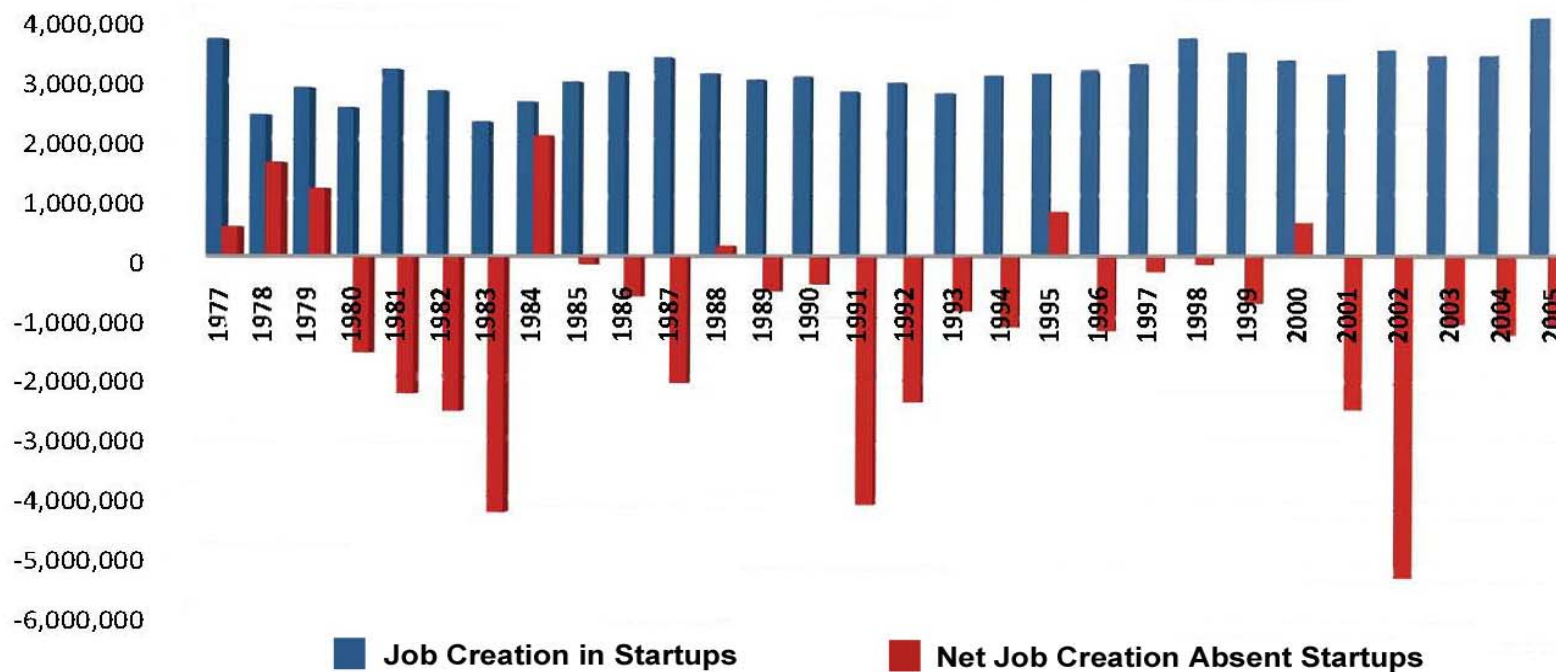
- In 2013, angels invested ~ \$25 billion in 71,000 companies
- Majority of net new jobs in US are from companies < 5 years old
 - High-growth startups create most of these jobs
 - Many receive angel funding prior to any VC investment
- Angels provide 90% of outside equity raised by startups
 - Virtually the only source of seed funding
 - 90%+ of VC goes for company expansion
- Angels deploy own funds and make own investment choices
- Approximately 200,000-300,000 active angel investors



...And Startups Create the Most Net Jobs

ENTREPRENEURS ARE KEY TO JOB CREATION

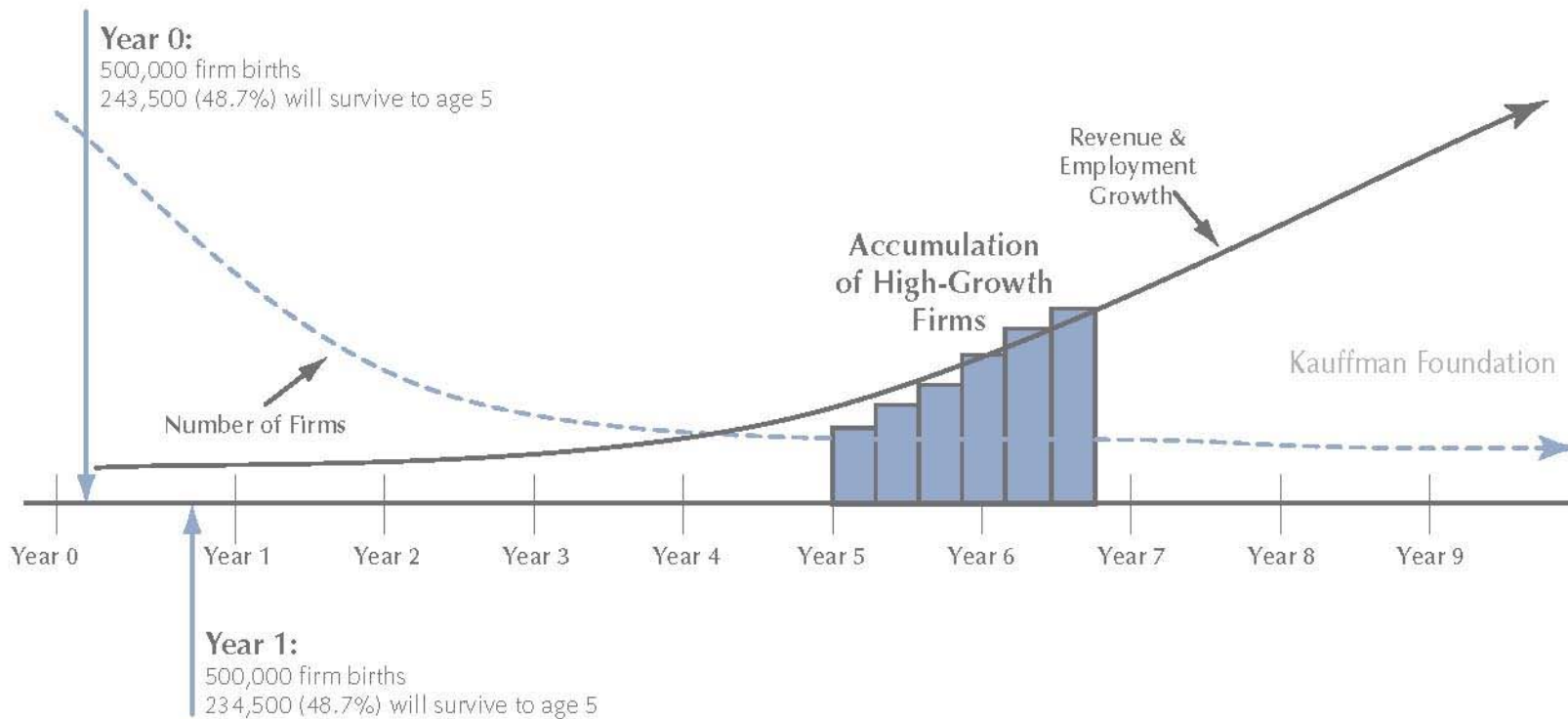
No Startups, No Job Creation



Source: Business Dynamics Statistics Briefing: Jobs Created from Business Startups in the United States. Kauffman Foundation, January 2009.

High-Growth Firms Build Jobs After Startup

Figure 7: The Accumulation of High-Growth Firms



Source: High Growth Firms and the Future of the American Economy, Kauffman Foundation, 2010



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Companies Backed by American Angels





Angels Fund Majority of Startups in USA

Angels Provide ~90% of Outside Equity for Startups

Angel Investors (2013)

- \$24.8 billion
- **71,000 deals**
- 32,000 seed
- 29,000 early stage
- 9,200 expansion
- > 298,000 individuals

Venture Capital (2013)

- \$29.6 billion
- **4,050 deals**
- 120 seed
- 1,375 early stage
- 2,550 later/expansion
- 548 active firms

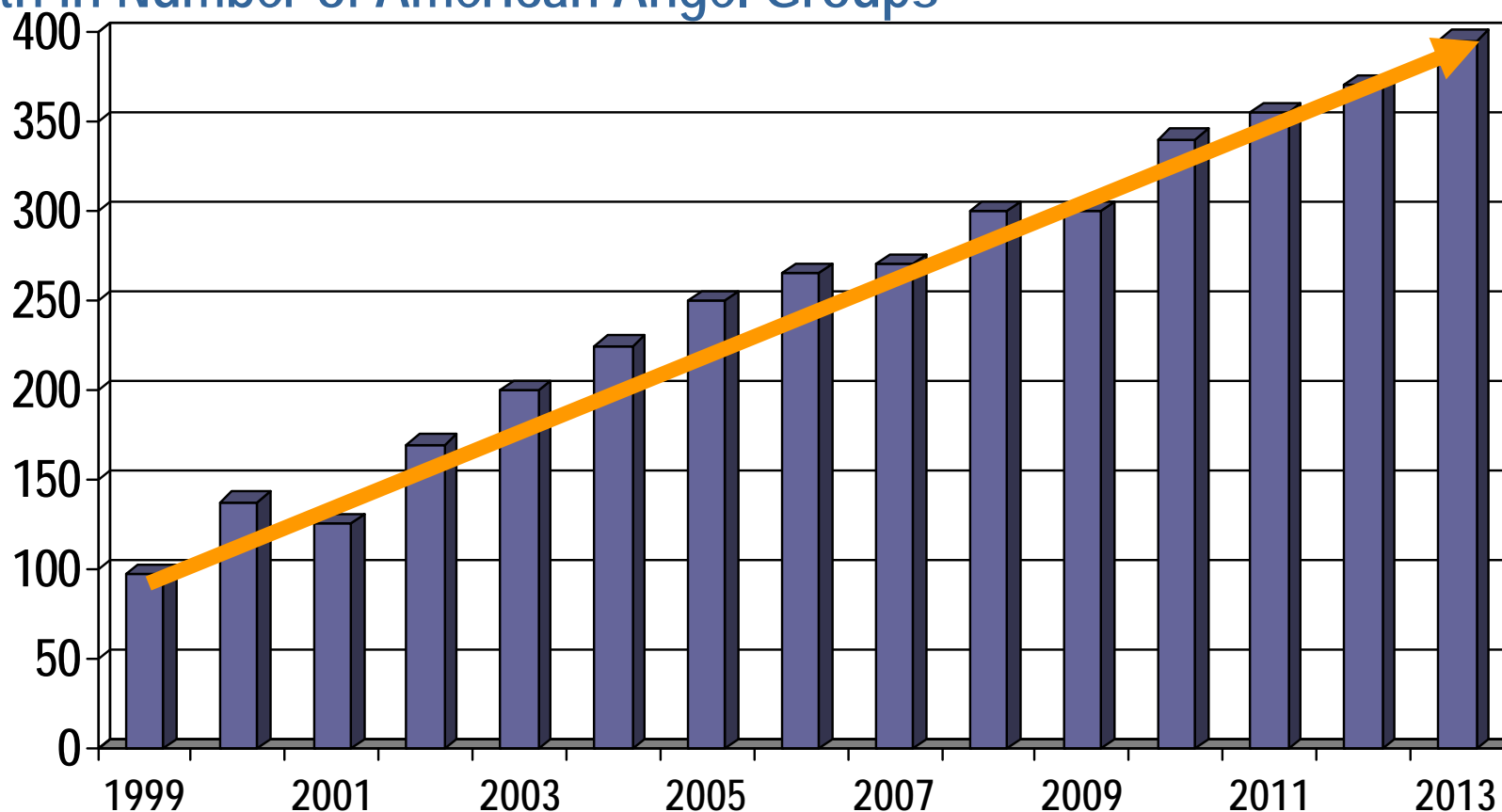
Sources: Center for Venture Research/ UNH; NVCA 2014 Yearbook; PwC MoneyTree



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Angel Groups are Key Trend in Sophisticated Investing

Growth in Number of American Angel Groups



Sources: Center for Venture Research (pre 03 data) and Kauffman Foundation/ARI (04-13 data)



Angel Investing = Hands-On Work

- Not just a check – ongoing support of entrepreneur
 - Customer acquisition
 - Personnel
 - Develop strategy
 - Resources: office space, accounting, etc.
- Work hand-in-hand
 - Economic development
 - University tech transfer
 - Accelerators/ incubators
- Active deal/risk assessment
 - Deal screening
 - ❖ Typically reject 90% that apply
 - ❖ Potential for growth/value creation
 - ❖ Fraud almost never an issue
 - Extensive due diligence
 - Negotiated terms – issuer does not set
 - ❖ Information rights
 - ❖ Board or observer seat
 - Intermediaries not involved
- Accredited platforms
 - Investors may follow a successful lead investor

Harvard/MIT study: angel support improves startup success rate



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Silicon Valley Bank



ANGEL RESOURCE INSTITUTE

present the

HALO Report™

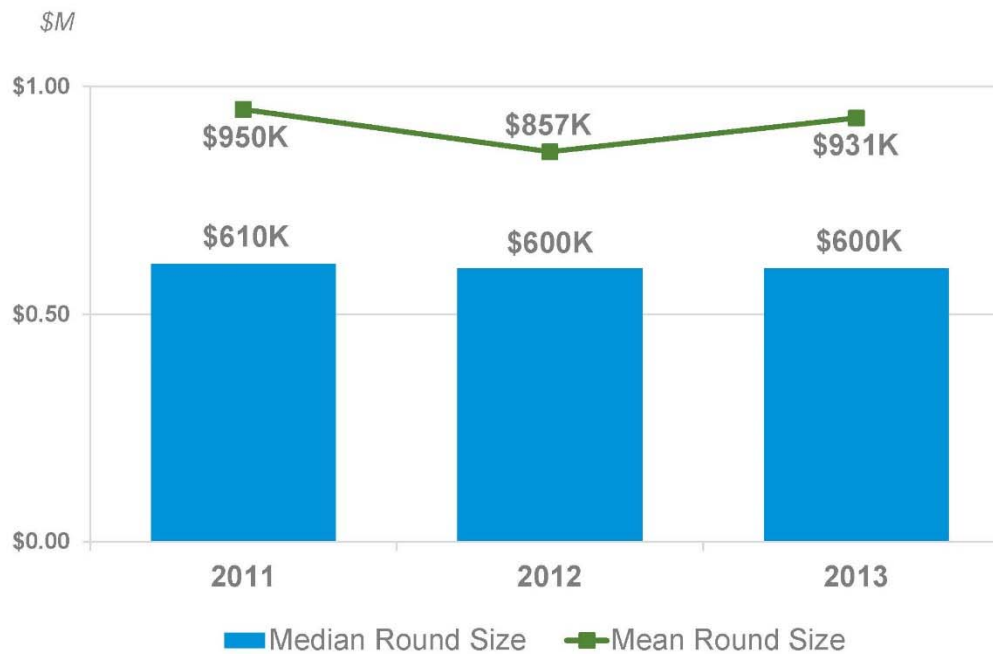


US Angel Group Update: 2013 Year in Review

Data Powered by CB INSIGHTS



Angel Round Sizes Remain Steady Over Three-Year Period



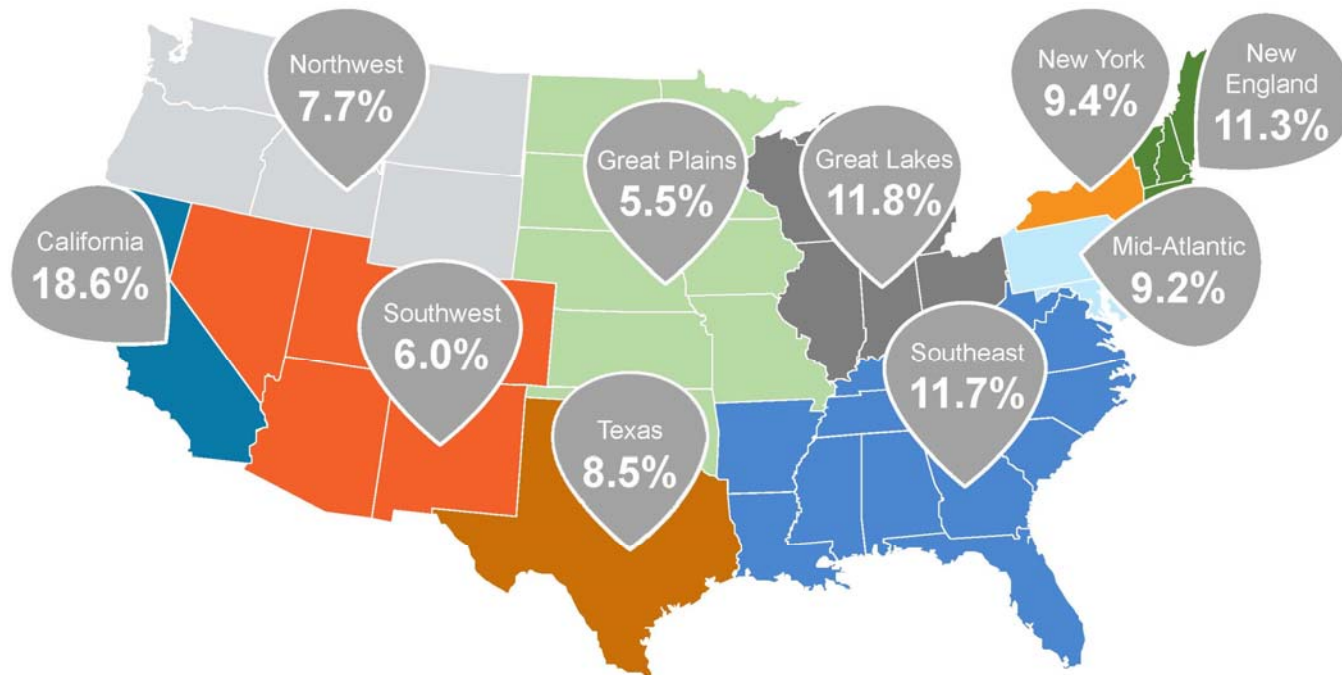
*Angel rounds include angels & angel groups only





Angel Group Deals are Widely Distributed Nationally

2013 Share of Angel Group Deals by Region





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Internet, Healthcare and Mobile Are Large Majority of Deals Investments In These Innovations 2/3 to 3/4 in Last Three Years

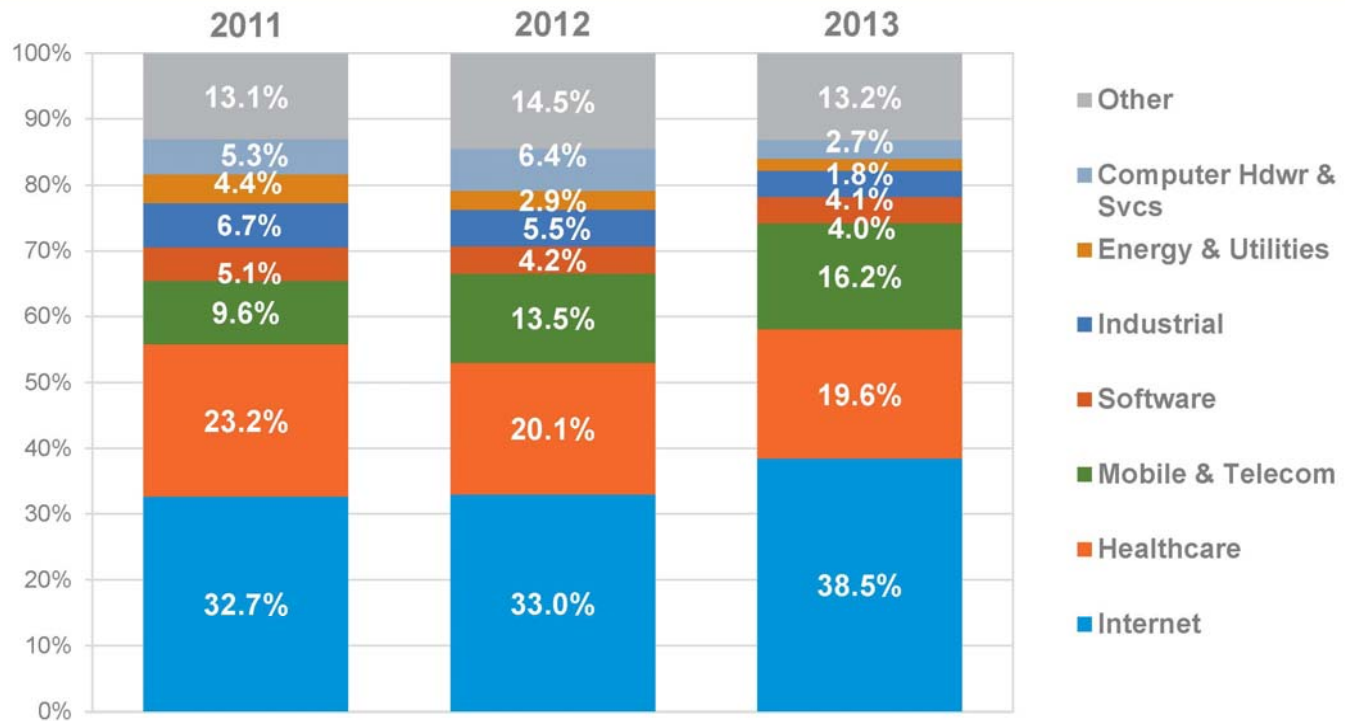


Chart references annual share of angel group deals across U.S.





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Top Sectors Claim Nearly 80% of Angel Group Dollars Mobile, Healthcare, and Internet

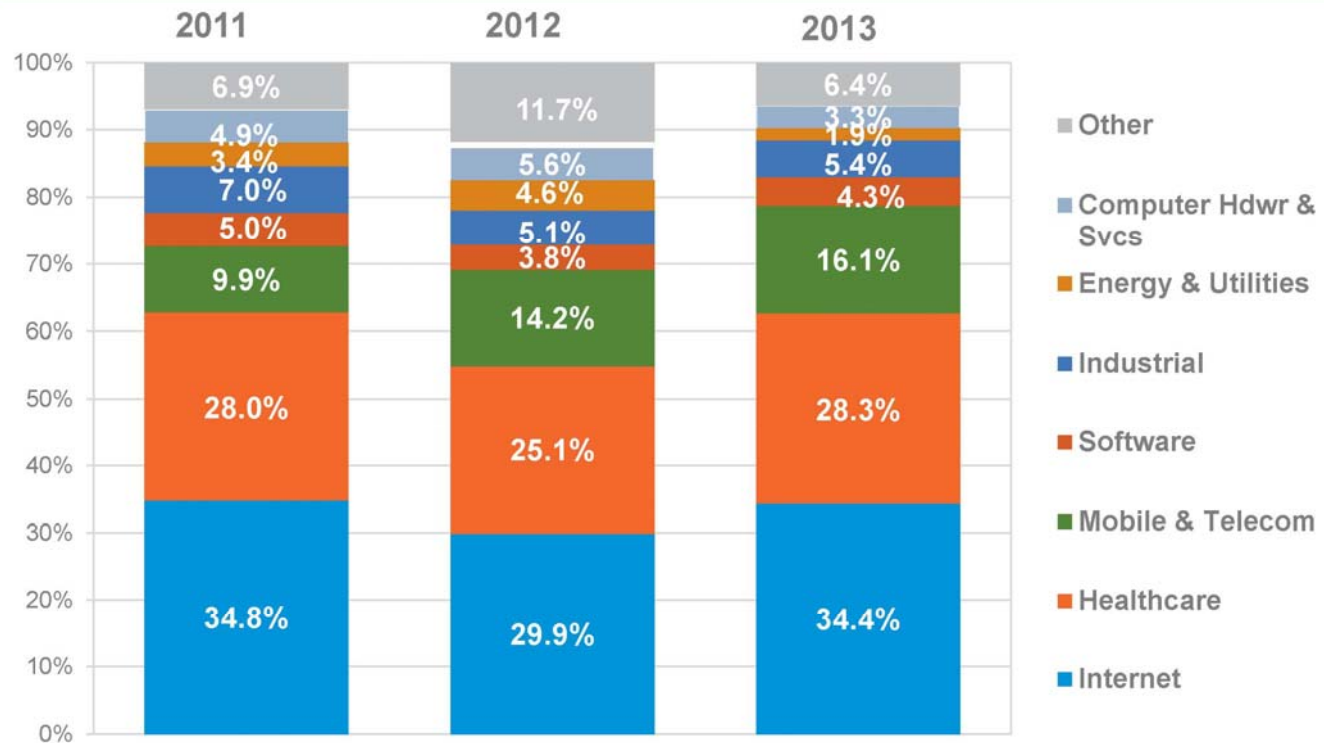


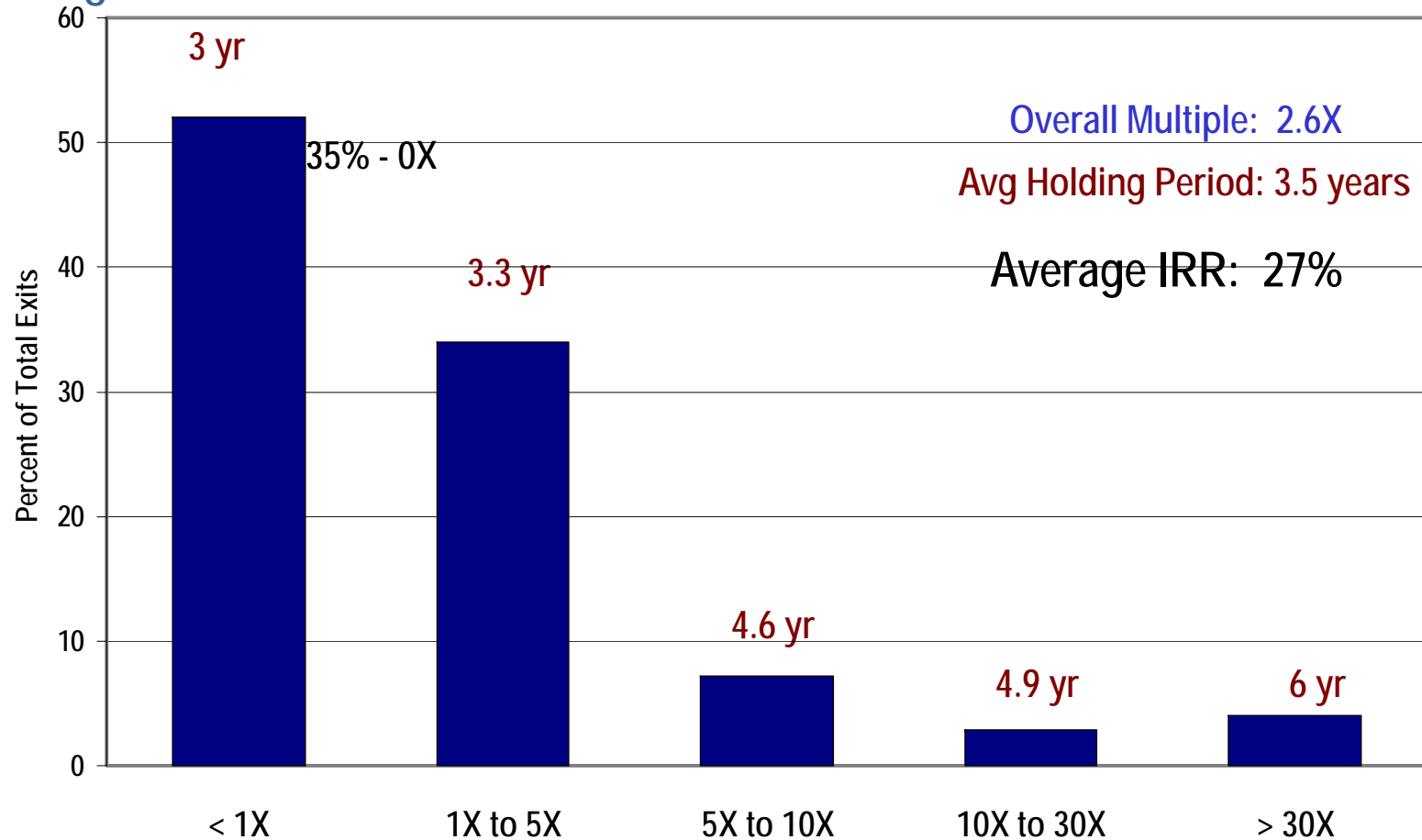
Chart references annual share of angel group dollars across U.S.





Angel Returns by Investment

Learnings Lead to Education & Best Practices



Source: Returns of Angels in Groups, 2007

Exit Multiples





Accredited Investor Definition Goals & Objectives

- Regulatory Objectives
 - Investor protection
 - Streamline capital formation for small business
 - Maintain market integrity
- ACA Goals
 - Preserve ability of knowledgeable investors to fund startups essential to job creation
 - Prevent undue obstacles to investor/entrepreneur relationship
 - Provide accredited investors education and best practices to enhance sophistication



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2010 Dodd-Frank Act Impact on Accredited Investor Standard

- Removing primary residence from net worth in 2011 was a major shift
 - Eliminated > 20% of eligible households
- 90% of Reg D deals had zero accredited investors
- Act says future reviews of definition should incorporate
 - Investor protection
 - Public interest
 - Economic environment (*in light of the economy*)
- Act tasks SEC only to review – not necessarily to alter



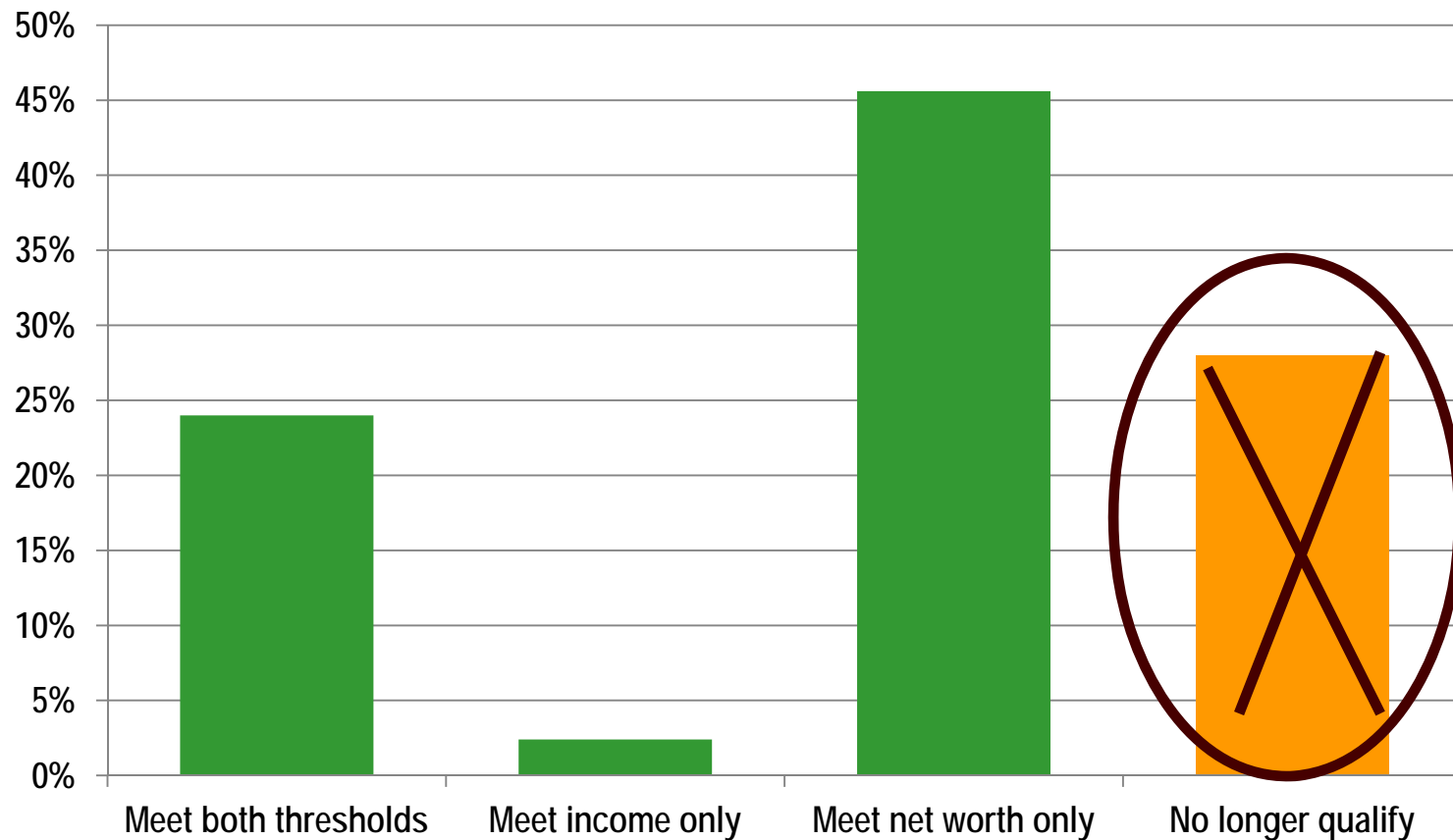
ACA Recommendation 1

- **Leave financial thresholds alone**
 - Clearly understood and worked well for decades
 - Removal of primary residence (2010) was significant shift
 - Private market too large and vital to further restrict investor access
 - Increases for inflation would have large market impact and reduce capital pool for entrepreneurs





28% of ACA Members Don't Meet Higher Thresholds



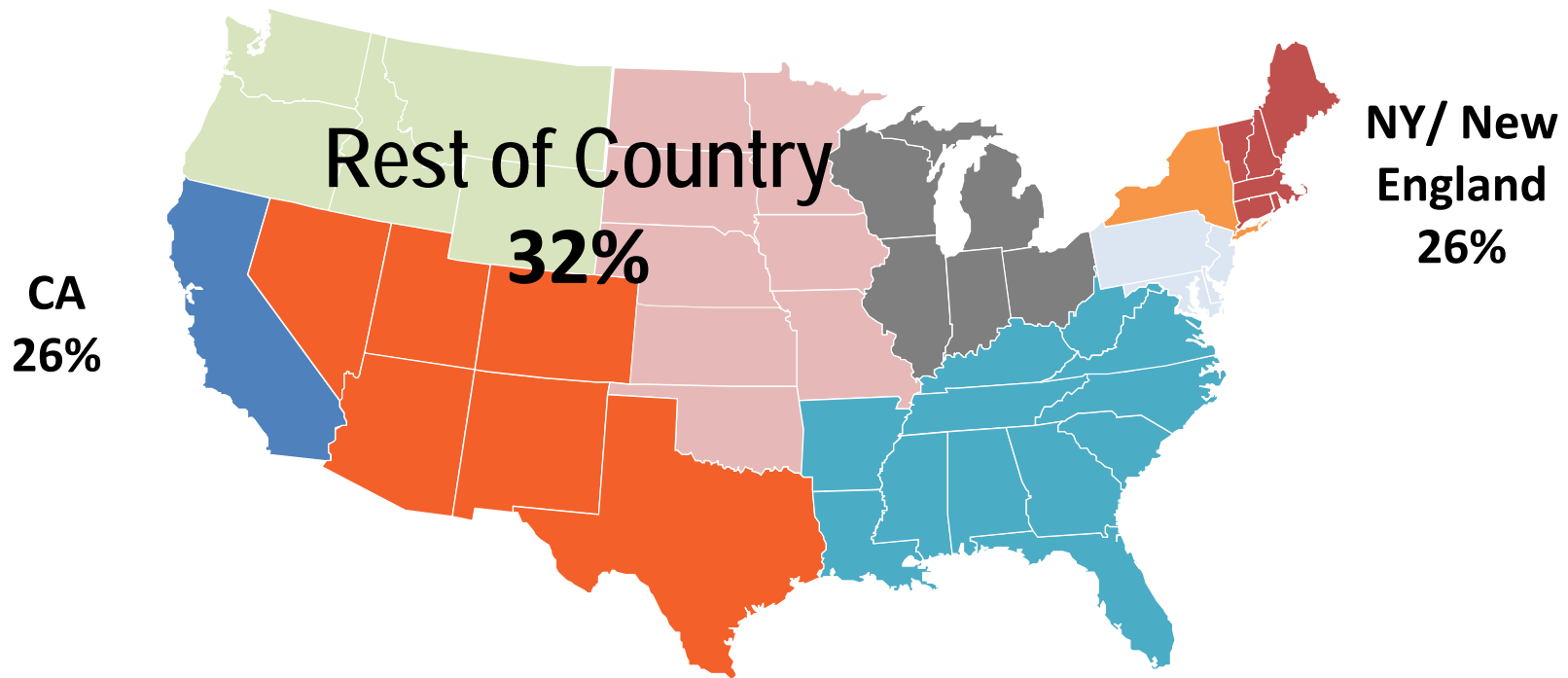
Source: ACA Survey, December 2013-January 2014 – 1009 members



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Impact of Raising Thresholds - \$2.5M / \$400K

% of ACA members who would not qualify



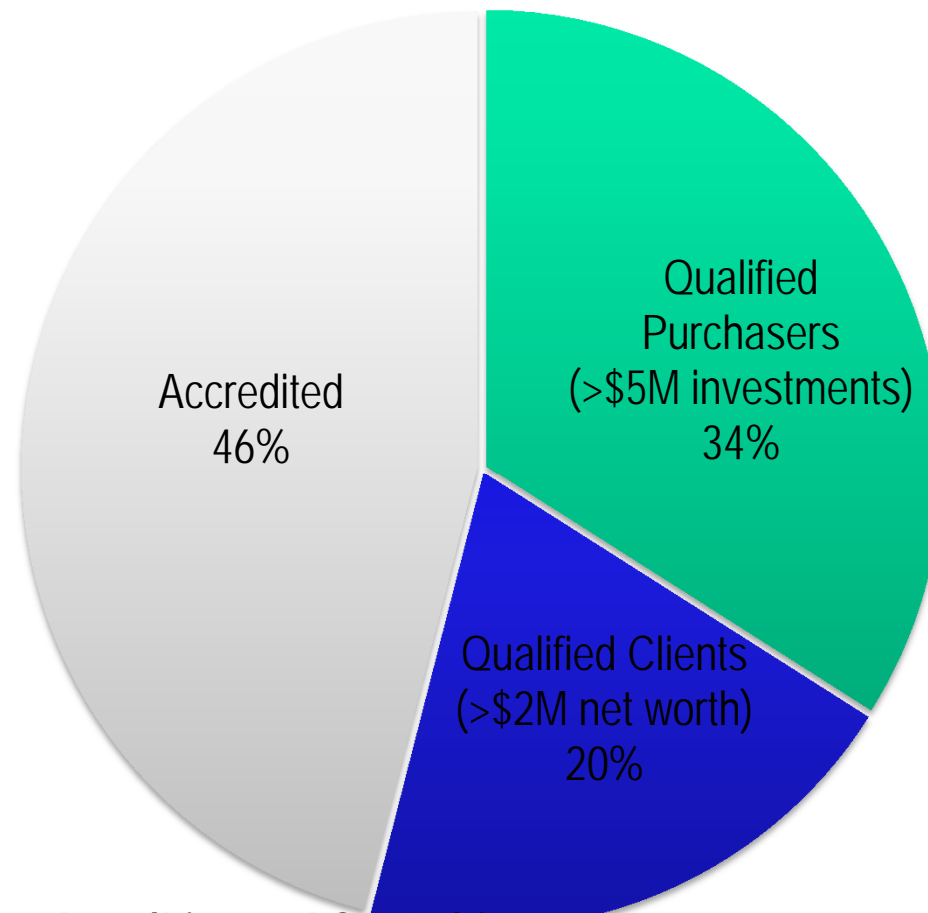
Nationwide, nearly 60% of accredited investors would cease to qualify (Source: GAO)

Map Data Source: ACA Member Survey, December 2013-January 2014



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Almost Half of AngelList Investors “Mere Accredited”



Source: Kevin Laws, AngelList on ACA Webinar, June 11, 2014



ACA Recommendation 2

- Add sophistication criteria to expand class
 - Prior board, executive or financial responsibility
 - Relevant degree or training: ACA certificate, MBA, JD, CPA, CFA, etc.
 - Previous experience with Reg D offerings
 - Membership in an Established Angel Group™
- Enable investors to certify via detailed questionnaire
 - Validates sophistication
 - Satisfy “issuer verification” for 506(c) deals
 - Reasonable simplicity of administration for all
- Once qualified as accredited investor, always qualified



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Sample Accredited Investor Qualifying Form

ACCREDITED INVESTOR TYPE

Which of the following, if any, applies to the investor:

- A natural person whose individual net worth, or joint net worth with spouse, exceeds \$1,000,000, not including primary residence.
- A natural person with individual income in excess of \$200,000 or joint income with that person's spouse of \$300,000 and who has a reasonable expectation of reaching the same income level in the current year.

INVESTOR BACKGROUND INFORMATION

Indicate which of the following categories, if any, applies to the investor. This information is sufficient to satisfy the issuer verification requirement regarding the accredited investor status of a purchaser.

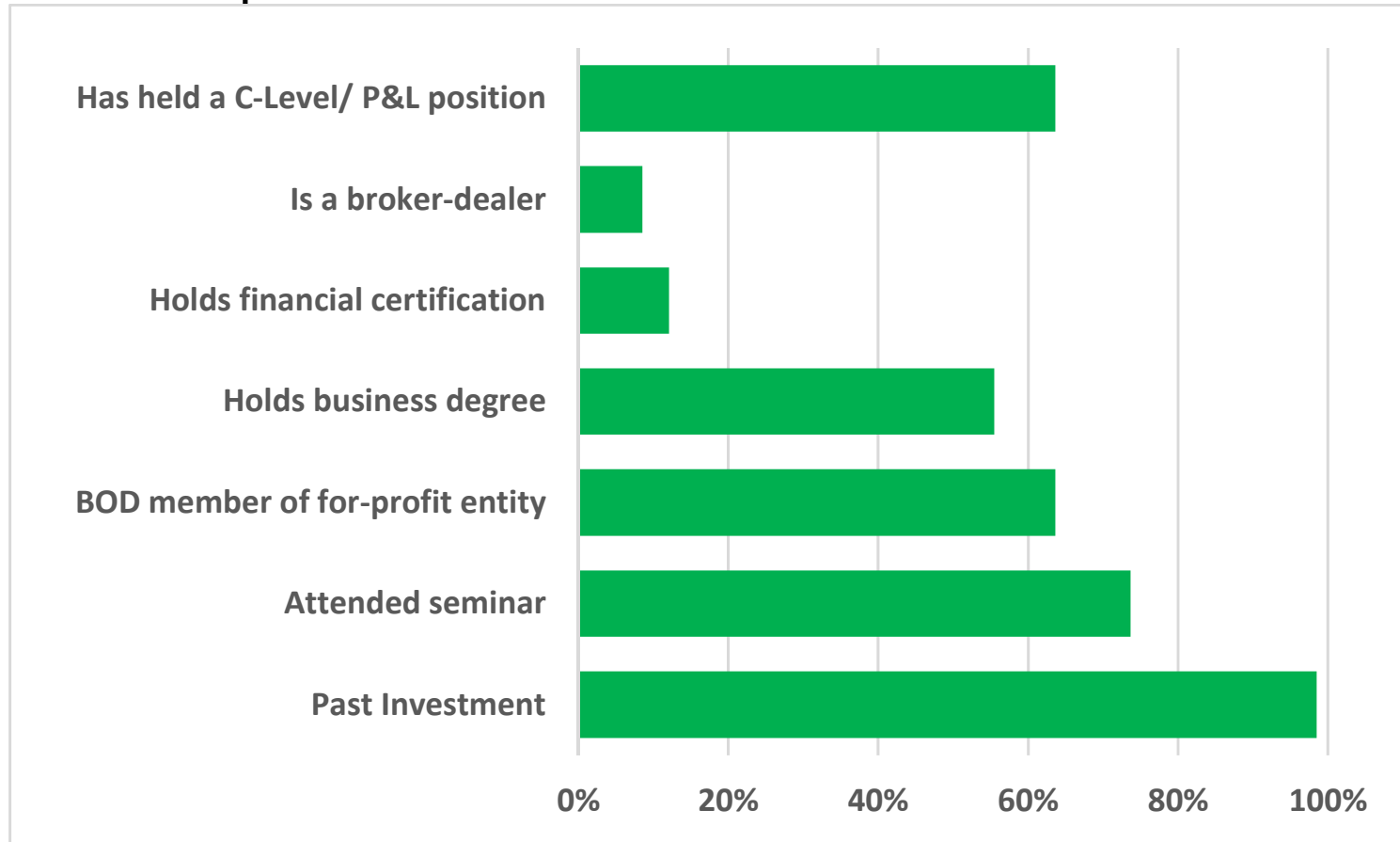
- Previous/current investor in an exempt offering under Regulation D
- Previous/current member of an Established Angel Group
- Previous/current C-Suite executive, financial officer or directors of a private or public for-profit entity
- Previous/current CEO or executive of a for-profit entity which included income statement responsibility
- Received a Certificate of Education from the Angel Capital Association, the Angel Resource Institute, or similar professional training from an Established Angel Group (EAG)
- Holder of relevant degree such as MBA, accounting, finance, etc. Please specify:
- Current or former holder of registration such as Certified Financial Adviser, Certified Public Accountant or similar registration. Please specify.
- Current or former registered broker dealer, financial advisor or similar.



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Common Sense Sophistication Measures

No Market Disruption / Investors Fend for Themselves

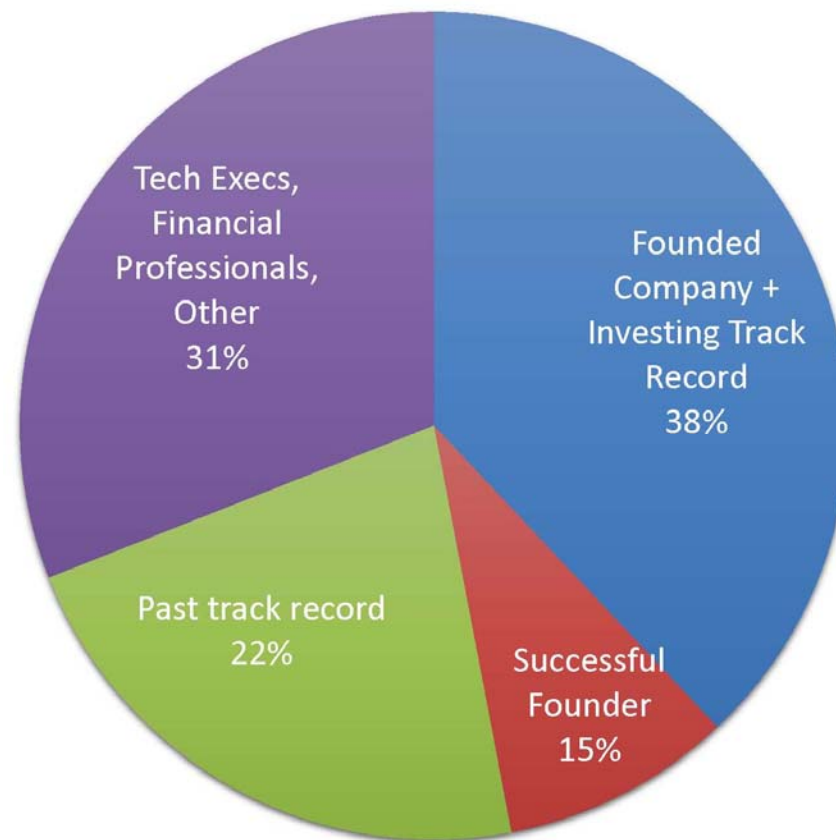


Source: ACA Survey, December 2013-January 2014 – 1009 members



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AngelList Investors Show Similar Sophistication



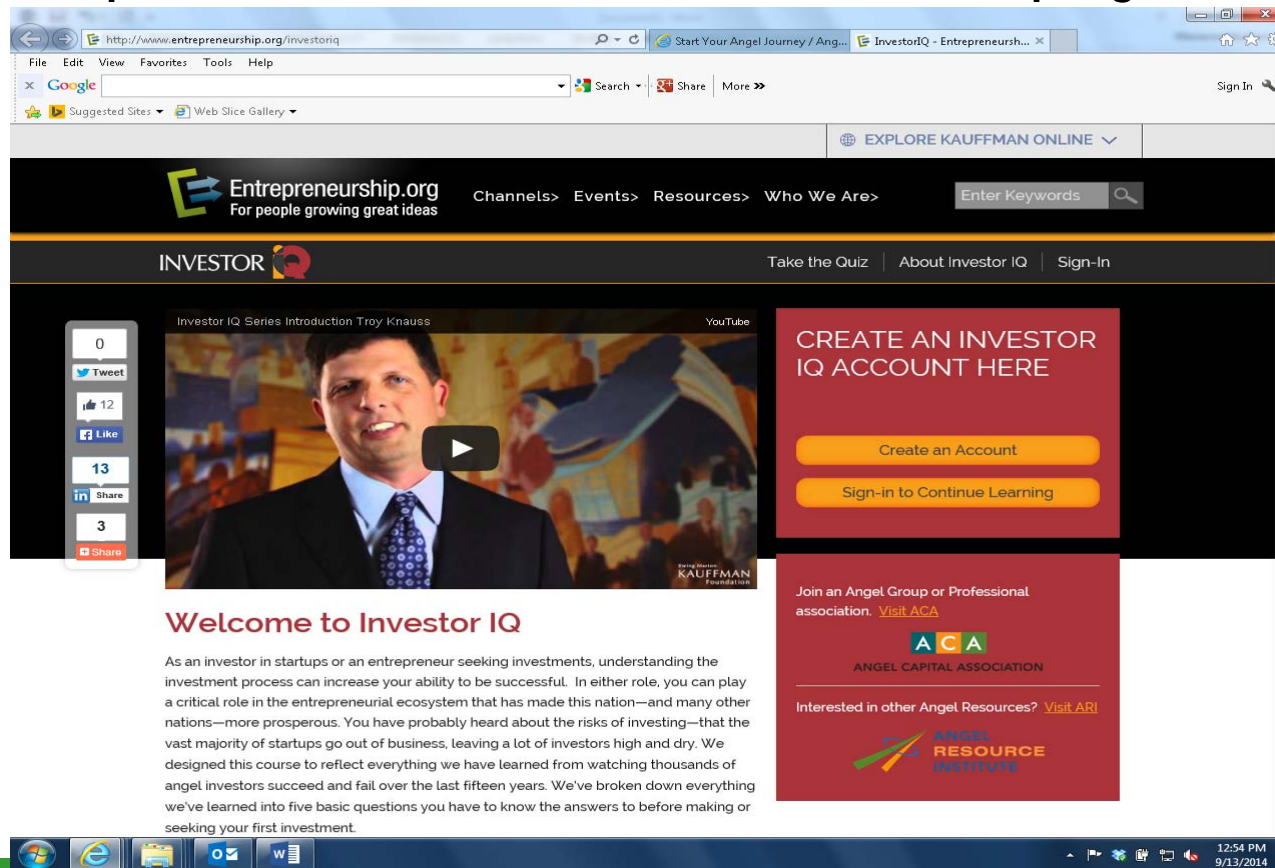
Source: Kevin Laws, AngelList on ACA Webinar, June 11, 2014



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ACA Recommendation 3

- Make investor education more widely known and available
 - Example: Kauffman Foundation's Investor IQ program





506(c) Issuer Verification Complicates Things

- Did issuer “solicit”?
 - University tech fair, economic development event
 - Accelerator pitch day
- Is investor accredited?
 - Financial thresholds – who will verify?
 - Reluctant 3rd parties, Investor privacy; data security; expense
 - Sophistication
 - Degree? Work experience? Established angel group member?
- Many groups will ONLY consider 506(b) – negating JOBS Act intent
- What kind of verification required for other ideas, like limiting investment to percentage of net worth?



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Comments on Investor Advisor Committee Recommendations

- Removing retirement assets from net worth calculation problematic
 - Many sophisticated angels invest from these accounts
 - Some advised to convert most assets into Roth IRAs, for example, by tax experts
- Do not implement proposed amendments to Regulation D and Form D
- Any revisions to definition should be phased in gradually so they don't sharply disrupt private markets



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More Information

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