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On Behalf Of
The Investment Program Association

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Good morning Chairman Garrett, Ranking Member Maloney, and members of the Subcommittee. My name is Wayne G. Souza, and I am General Counsel and Executive Vice President of Law of the Walton International Group of Scottsdale, Arizona. I am pleased to be here today to testify on behalf of the Investment Program Association.

The Investment Program Association (IPA) was created in 1985 to serve as a national trade association for the Direct Investment industry. We offer leadership, education and advocacy services to more than 150 corporate members, who include securities product-offering sponsors, broker-dealers, and Direct Investment service providers.

"Direct Investment" refers to the business activity of individuals who pool their capital with other investors to make direct investments in tangible assets without taking on management or operational responsibilities. The IPA's members facilitate the transfer of capital between investor and business without the intermediary function of a stock exchange or bond underwriter. Examples of direct investment products include non-listed real estate investment trusts (REITs), oil and gas programs, equipment leasing programs, private placement securities offerings in real estate, and business development companies (BDCs), with BDCs constituting a fast-growing segment of the IPA's membership.

The vast majority of direct investment products are designed to be medium- to long-term holdings, and are therefore seldom traded as compared to various exchange-traded investments. Because they are intended to be held for longer durations, these products offer critically important capital in the form of stable equity and debt investments, reducing volatility in the marketplace. Direct investment products own dozens of types of tangible assets that touch the daily lives of Americans and facilitate job creation and retention. These investments are represented in the ownership of hotels, drug stores, skyscrapers, timberland, master-planned

community developments, theme parks and senior living facilities, to name just a few. At year-end 2012, direct investments represented more than $100 billion in assets under management, in more than 1.5 million investor accounts, with an average investment of $30,000. The IPA's members reported total sales of $13.3 billion in 2012, with the vast majority of that, $10.3 billion, in non-listed REITs and $2.8 billion in business development companies.

My own organization, the Walton International Group, is a real estate investment and development company that focuses on the research, acquisition, management and development of real estate assets across North America. Our goal is to achieve the highest and best development potential of the land while maximizing returns for our investors. Walton currently manages more than $3.5 billion in assets, including more than 74,000 acres of land in North America, and our affiliates have managed privately offered real estate programs involving North American lands for more than 85,000 investors worldwide.

The direct investments facilitated by Walton International and the other members of the IPA are an invaluable and irreplaceable source of capital for America's small businesses, and that capital creates and sustains employment in America. Therefore, we are especially pleased to have this opportunity to discuss ways to reduce barriers to capital formation, and we applaud the Subcommittee for taking the time to consider this topic. No topic is more important to small businesses, which as you know are the primary source of new jobs in the U.S. economy.

The JOBS Act's Impact on Direct Investment

We commend Congress and this Subcommittee for the major work you have already done to stimulate the growth of small to midsized companies through the enactment of the Jumpstart Our Business Startups (JOBS) Act last year. The JOBS Act included quite a few

provisions that will foster the creation of new businesses and the growth of existing ones, and facilitate the movement of capital within the marketplace.

Key provisions of the JOBS Act reduce unnecessary regulatory burdens on direct investment products and their providers, and make it easier for small businesses to find new investors and new sources of capital. Specifically, we applaud the creation of the new category of "emerging growth companies," with a streamlined route to initial public offerings (IPOs); the removal of the ban on general solicitation and advertising for certain offerings under Regulation D, Rule 506 and Rule 144A; the increase in the amount of capital that small businesses can raise without triggering the SEC's registration requirements; and the expansion of the number of shareholders a small business may have without being required to commence a SEC registration process. All of these provisions make it easier for small businesses to raise capital within their communities and from other interested investors.

In considering additional legislative changes to pursue those goals even further, the IPA can suggest some clarifications to these provisions that will make them even more effective.

Clarify the "Testing the Waters" Provision

Title I of the JOBS Act offers an "IPO On-Ramp" that makes it easier for private companies designated as "emerging growth companies" to seek capital through an initial public offering (IPO). The creation of this new category is a valuable change that will make new capital more readily accessible to thousands of growing enterprises.

Among the provisions that empower these emerging growth companies is Section 105(c), the so-called "testing the waters" provision. This section allows an emerging growth company or its authorized representative to engage in oral or written communications with qualified

institutional buyers or accredited investors without becoming subject to the requirements that apply to prospectuses under Section 10(a) of the Securities Act.

As we have begun to implement the JOBS Act, however, it has not been sufficiently clear that these "testing the waters" materials used by emerging growth companies are exempt from the requirements that apply to public offerings. This risk is one of perception rather than reality, but the lack of clarity creates a chilling effect in the marketplace, as emerging growth companies may be reluctant to avail themselves of the Act's provisions.

Existing law offers a precedent for clarifying this perception. Rule 408(b) under the Securities Act of 1933 explicitly states that "the failure to include in a registration statement information included in a free writing prospectus will not, solely by virtue of inclusion of the information in a free writing prospectus . . . be considered an omission of material information required to be included in the registration statement." This provision clarifies that the information in a free writing prospectus is not necessarily identical to that in an eventual registration statement. Similar language applied to the "testing the waters" provision of the JOBS Act would reassure both emerging growth companies and the market, and encourage the use of this provision.

Clarify Provisions on General Solicitation and General Advertising

Title II of the JOBS Act required the SEC to develop rules to establish steps for issuers of securities to make sure that securities sold through a general solicitation or by general advertising are sold only to accredited investors. The Commission's rulemaking process has proven complex, and is taking considerable time to complete.

Certain members of the regulatory community have urged the SEC to include content and disclosure requirements as part of its rules governing solicitation and advertising to accredited investors. We respectfully submit that Title II of the JOBS Act grants the SEC no new authority to set content standards. In our view, the Congressional request was clear: the SEC is to establish steps by which an issuer can verify that sales of securities resulting from solicitation and advertising have been made only to accredited investors. The authority to impose these verification steps does not include the authority to impose content standards for solicitation and advertising materials. Congress should facilitate this process by clarifying provisions in Title II of the JOBS Act to make clear Congress's intent that the Act neither requires nor permits the SEC to adopt any disclosure requirements or content standards with regard to advertising and solicitation materials for accredited investors.

It might also be helpful for Congress to provide guidance on the disqualification and other treatment of so-called "bad actors" who violate these requirements under Dodd-Frank.

Reduce Compliance Burden on Business Development Corporations

One of the fastest-growing segments of the IPA's membership is business development corporations (BDCs), which are publicly traded and privately held private equity organizations that invest in growing US-based businesses. They are governed by the Investment Company Act of 1940. BDCs are similar in function to venture capital and other private equity firms, but their ownership structure makes them accessible to the general public, and allows them to offer small investors a way to participate in the capital markets. BDCs can play tremendously important roles in their community by moving capital quickly to businesses with urgent needs, as we saw the New York Business Development Corporation do in the wake of Hurricane Sandy.

A provision to streamline BDCs' registration statement filing requirements with the SEC, by allowing them to incorporate by reference from reports already filed with the SEC, would reduce duplication of effort and unnecessary regulatory burden. It would free up time, attention and compliance costs to make those resources available for additional support to emerging businesses.

We note that this suggestion is one of several provisions included in both H.R. 1800, the Small Business Credit Availability Act, introduced by Representative Michael G. Grimm, and H.R. 31, the Next Steps for Credit Availability Act, introduced by Representative Nydia Velazquez. This bipartisan legislation would give BDCs greater access to capital by amending the Investment Company Act of 1940 to allow BDCs to own investment adviser subsidiaries. It would also raise the reasonable leverage cap amount placed on BDCs, and would allow BDCs to count preferred stock as equity rather than debt in calculating total leverage. These changes, if implemented, would have the ultimate effect of enhancing a BDC's ability to raise funds and to lend or invest these funds to small and mid-size American businesses.

We further applaud several other provisions of H.R. 31/H.R. 1800, including the proposal to extend the definition of "well-known seasoned issuer" to include BDCs and the proposal to add registration statements filed on Form N-2 to the definition of automatic shelf registration statement, both provided by Rule 405.

Encourage State Acceptance of Electronic Signatures

A continuing challenge to our members as they try to match investors with businesses looking for capital is existing state laws that do not acknowledge the legitimacy of electronic signatures in executing the sale of certain securities products in all jurisdictions. While we

recognize states' legitimate interests in these transactions, these different state requirements and in some cases prohibitions slow down and block the free movement of capital between regions. The 2000 Electronic Signatures in Global and National Commerce Act expressed the intent of Congress to utilize electronic signatures in the conduct of commerce. We recommend that Congress consider updating the securities laws to allow the acceptance of electronic signatures on securities subscription documents in all jurisdictions.

Beyond these recommendations, our members see many opportunities to facilitate and encourage capital investment through changes to the federal tax code. Although these changes fall outside this Subcommittee's jurisdiction, we look forward to opportunities to discuss these changes with individual members and the appropriate Committee in future.

Conclusion

Once again, I thank the Subcommittee for this opportunity to share the views of the Investment Program Association. Every day our members work in partnership with real estate developers and other small businesses to create economic opportunities in the communities where we live. We help individual investors put their money to work directly in their communities, and our business is built on trust and stability. We value our reputation for integrity and fair dealing, and we appreciate the work this Subcommittee is doing to promote the free flow of capital in our economy.

As you continue this effort, please call on us for additional information and support. We look forward to working with you. I would be pleased to answer any questions the Subcommittee members may have.