# David Weild: The Father of the JOBS Act Has a 'Magic Bullet' for Small-Caps

## By Adam J. Epstein

David Weild IV (*pictured*) is the founder of Weild & Co., an investment banking firm that assists public or aspiring public companies with capital formation and aftermarket support to expand their distribution to select investors. Weild previously was vice chair and executive committee member of Nasdaq and spent 14 years at Prudential Securities in various senior management positions including head of corporate finance, technology investment banking, and global equity capital markets.

Weild and a colleague conducted studies between 2008 and 2011 that documented the long-term decline in equity capital formation in the United States and provided the core arguments that gave rise to the Jumpstart Our Business Startups (JOBS) Act. Weild has testified before Congress and the Securities and Exchange Commission (SEC) on these and other market issues. In 2013, he authored a study for the Organisation of Economic Co-operation and Development (OECD) titled "Making Stock Markets Work to Support Economic Growth," and presented it to the 35 member nations of the OECD, as well as the European Commission. In 2015, he addressed the G-20 in Istanbul and co-authored the study "The U.S. Need for Venture Exchanges."

***You're widely regarded as the father of the JOBS Act. Why was there a need for the JOBS Act?***

The entrepreneurial economy in the United States was in trouble. American start-ups historically accounted for most [of the] job growth in the U.S., but beginning in 1998, the small initial public offering [IPO]—i.e., IPOs that raise less than $50 million, or $84 million when adjusted for inflation—dropped off a cliff and never recovered. If companies can't go public until much later in their life cycles, more businesses get acquired, jobs are shed, returns on start-up capital decline, and investors cut their allocations of capital to earlier-stage companies. According to Gallup, the percentage of U.S. start-up companies (defined as less than one year of age) in 1978 was 16.5 percent of all companies. Today, the percentage of start-ups has been cut in half and is only 8 percent of all companies. During the credit crisis, for the first time in history American businesses were being destroyed at a faster rate than they were created. We believe that reestablishing access to capital and support for private and public companies is at the very core of what will make America great again.

***Where are we today with implementation of the JOBS Act?***

It has been four years since the JOBS Act was signed by President Obama. I was in the Rose Garden for the April 5, 2012 signing of the Act along with a large group that included politicians, congressional staff, stock exchange executives, and crowdfunding proponents. Unfortunately, the way that the Act was written, most of the Act was ceded to the SEC for rulemaking, which caused years of delays since the SEC was already overwhelmed by rulemaking for Dodd-Frank. The first five titles (there are seven titles total) are having the greatest impact on our capital markets:

- **Title I.** The establishment of a new category of public issuer, the "emerging growth company," that was given the ability to pre-market an IPO to institutional investors ("testing the waters"), the ability to "confidentially file" a registration statement without the public being able to view its contents until the IPO was ready to go, and a form of scaled-in-regulations, to curtail up-front compliance costs.
- **Title II.** The ability to "generally solicit" (i.e., market) Regulation D private placements under certain circumstances, now encapsulated by Rule 506(c).
- **Title III.** The so-called crowdfunding provision that will finally go into effect on May 16 and enable issuers to raise up to $1 million from the public with significantly lower costs than a traditional public offering.
- **Title IV.** Known as "IPO lite" in some quarters, Regulation A+ allows companies to raise up to $50 million in capital under a lower-cost disclosure regime, and is being co-opted for larger crowdfunding deals.
- **Title V.** This provision raised the number of shareholders that a company is permitted to have from 500 to 2,000 before it is required to register and become a reporting company with the SEC. It's arguable that Title V has added fuel to the "unicorn" phenomenon of

private companies with valuations that exceed $1 billion, because it allows companies to stay private longer. It has been reported that Facebook had to go public because it tripped the previous 500-shareholder limit, so some refer to Title V as "The Facebook Rule."

***Why has the number of exchange-listed companies in the U.S. declined in the last 20 years, and why does that matter?***

In 1998, the SEC drove higher price competition in equity trading in the form of a mass transition from telephone-quoted quarter-point spread markets to low-cost electronic stock markets; the rule was known as Regulation ATS (Alternative Trading System). The ensuing collapse in trading economics caused traders to lose money supporting stocks, so Wall Street started pulling resources away from small-cap companies and the small IPO market. The ecosystem of firms that supported small-cap stocks and small IPOs collapsed. The lack of IPOs and the lack of support then caused the number of listed companies to decline from roughly 9,000 in 1997 to 5,000 today. (We estimate that if market structure remained unchanged, that the U.S. would have nearly 14,000 listed companies today.) Why does it matter? It matters because the U.S. likely lost over 10 million jobs in the process. The timing of this period suspiciously overlaps with our employment problems and our decline in wage/labor rates. The poor are poorer. The middle class has seen a decline in income. Upward mobility has declined. The American Dream was turned into a bit of a nightmare. So, yes, it matters. I think getting the entrepreneurial growth economy and small IPO market back on track is one of the most important things that we can do to secure better opportunity and quality of life for the next generation.

***You were a driving force behind the SEC's forthcoming pilot program to widen the minimum quoting and trading increments, or tick size, of smaller company stocks. Why do tick sizes matter, and what can we expect the pilot to achieve?***

The JOBS Act is really, at best, only half of the required solution. What is needed now is aftermarket support for small public companies and the return of an ecosystem of small investment banks required to provide banking expertise, equity research coverage, distribution (sales), and market-making support. It is an inconvenient truth that as markets become lower-cost and electronic, smaller-capitalization stocks lose support and liquidity, and that professional investors abandon these stocks in favor of larger, innately liquid stocks. The rich (large-cap companies) get richer and the poor (small-cap companies) get poorer. Increasing tick sizes (a tick is the minimum increment in which a market maker can quote a stock) to something higher than the current one penny a share is critical to bringing back interest in supporting small-cap stocks. While a penny is enough incentive for a large-scale liquid stock like Apple that trades tens of millions of shares a day, it is totally inadequate for stocks that trade with little to no liquidity. The SEC is going to test five cents a share as a minimum tick size in smaller stocks. We think it should have tested ten cents and even higher. Our work for the OECD demonstrated that you really need tick sizes that account for 1 percent or more of share price, on average, to pay for the ecosystem of investment banks required to drive the small IPO market.

***The capital markets seem to be sized more for large-cap companies, despite the fact that the overwhelming majority of public companies are small. How can the U.S. ultimately make capital markets work for smaller public companies?***

We proposed the solution in a *Wall Street Journal* op-ed that appeared on Oct. 28, 2011. In the piece titled "How to Revive Small-Cap IPOs" I wrote: "What's needed now is a new, parallel market for public companies under $2 billion in value. Trading rules in this new market would allow for higher commissions, which would provide adequate incentives for small investment firms to get back into the business of underwriting and supporting small-cap companies. The SEC could use its authority under securities laws to exempt this market from rules standing in the way, or Congress can step in." The chair of the House Subcommittee on Capital Markets and Government Sponsored Enterprises, Scott Garrett (R-NJ) actually introduced such a bill to the House Financial Services Committee on March 3. It is called the Main Street Growth Act, and it would amend the Securities Exchange Act of 1934 to create a new form of "national" stock exchange (exempt from state regulation the way NYSE and Nasdaq stocks are exempt from state "blue sky" regulation) that would be optimized for the unique needs of small-cap companies in the aftermarket.

It is an idea that is long overdue. It is the magic bullet for free enterprise. And, while it would take a long time to build back the infrastructure required, such a "venture exchange" construct would help to secure America's competitive footing. The very fact of one-size-fits-all markets (today's electronic markets are fit for large-cap trading but unfit for small public companies) has created, in my view, the biggest economic catastrophe in my lifetime. The damage exceeds that of even the credit crisis.

Adam J. Epstein was an institutional investor who now advises pre–IPO and small-cap boards through his firm, Third Creek Advisors LLC. He is the author of *The Perfect Corporate Board: A Handbook for Mastering the Unique Challenges of Small-Cap Companies* (McGraw-Hill, 2012).