MANAGED FUNDS ASSOCIATION
The Voice of the Global Alternative Investment Industry
WASHINGTON, DC | NEW YORK

September 28, 2012

VIA EMAIL

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings

Dear Ms. Murphy:

Managed Funds Association ("MFA")[1] appreciates the opportunity to provide comments to the Securities and Exchange Commission (the "SEC" or "Commission") in response to its proposal to implement Section 201(a) of the Jumpstart Our Business Startups Act (the "JOBS Act").[2] This letter follows comments we submitted in advance of the proposal, which are attached.[3]

We believe the amendments to Rule 506 of Regulation D in the JOBS Act will have beneficial effects for investors, regulators and the hedge fund industry. In particular, eliminating the ban on general solicitation will reduce legal uncertainty, facilitate capital formation, and increase transparency of the hedge fund industry in a manner consistent with the Dodd-Frank Act, while maintaining strong investor protections and ensuring that only sophisticated investors are able to

[1] The Managed Funds Association (MFA) represents the global alternative investment industry and its investors by advocating for sound industry practices and public policies that foster efficient, transparent, and fair capital markets. MFA, based in Washington, DC, is an advocacy, education, and communications organization established to enable hedge fund and managed futures firms in the alternative investment industry to participate in public policy discourse, share best practices and learn from peers, and communicate the industry's contributions to the global economy. MFA members help pension plans, university endowments, charitable organizations, qualified individuals and other institutional investors to diversify their investments, manage risk, and generate attractive returns. MFA has cultivated a global membership and actively engages with regulators and policy makers in Asia, Europe, the Americas, Australia, and all other regions where MFA members are market participants.

[2] Section 201(a)(1) instructs the SEC to revise Rule 506 of Regulation D under the Securities Act of 1933 to eliminate the prohibition against general solicitation or general advertising for offers and sales of securities made pursuant to Rule 506, provided that all purchasers are accredited investors.

[3] Letter from Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel, MFA, to Elizabeth Murphy, Secretary, SEC (May 4, 2012), available at: https://www.managedfunds.org/wp-content/uploads/2012/05/MFA_Comments_on_JOBSAct_05-04-2012.pdf; Letter from Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel, MFA, to Elizabeth Murphy, Secretary, SEC (June 26, 2012), available at: https://www.managedfunds.org/wp-content/uploads/2012/06/MFA-Comments-on-JOBS-Act-6-26-12.pdf.

purchase interests in private funds.[4] MFA has consistently opposed any policies that could lead to a "retailization" of traditional hedge fund products, and we continue to maintain our longstanding position in support of proposals that would heighten the qualification requirements of investors in hedge funds.[5] Following implementation of the JOBS Act, investments in hedge funds will continue to be restricted to sophisticated individuals and institutions.

Section 201(a)(1) directs the SEC to include in its rule a requirement that an issuer take reasonable steps to verify that purchasers of securities offered and sold under revised Rule 506 are accredited investors. The SEC has proposed that an issuer seeking to engage in general solicitation should comply with this requirement by conducting an analysis of the facts and circumstances of each transaction. Under the proposed approach, an issuer would consider characteristics of the transaction – such as the nature of the purchaser, the information it has about the purchaser, the solicitation method, and the minimum investment amount – and determine the types of verification methods that would be reasonable in light of these characteristics.

In general, we believe the proposal is an effective approach, and will enable issuers to implement appropriate measures to meet the requirements of Section 201. As we have previously noted, we understand that the SEC must implement the JOBS Act in a manner that addresses the needs of a variety of constituencies, and we recognize that there are categories of prospective investors who may need additional attention by issuers. At the same time, it is important that issuers are able to take steps to verify the status of purchasers in a practical, efficient manner, particularly in contexts where investors are often large institutions or individuals with substantial assets. An overly prescriptive approach to verification would undermine the clear intent of the JOBS Act to modernize private offerings and enhance capital formation.

As such, we commend the SEC for proposing a framework to implement Section 201 that permits issuers to use a variety of methods to verify the status of purchasers. We believe the proposed facts and circumstances analysis fulfills the SEC's statutory mandate to determine the methods that an issuer should use in taking steps to verify the status of investors, and provides appropriate protection for investors.[6] A one-size-fits-all approach to verification would be inappropriate for the many different types of institutions and individuals who will seek to invest in offerings conducted pursuant to new Rule 506(c).

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[4] For a complete discussion of these effects, *see* Rulemaking Petition from Richard H. Baker, President and CEO, MFA, to Elizabeth Murphy, Secretary, SEC (Jan. 9, 2012), available at: http://www.sec.gov/rules/petitions/2012/petn4-643.pdf.

[5] *See* Letter from Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel, MFA, to Elizabeth Murphy, Secretary, Securities and Exchange Commission (July 8, 2011), available at: http://www.managedfunds.org/wp-content/uploads/2011/09/MFA-Comments-on-Qualified-Client-Proposal.pdf; Letter from Richard H. Baker, President and CEO, MFA, to Elizabeth Murphy, Secretary, SEC (Mar. 11, 2011), available at: http://www.managedfunds.org/wp-content/uploads/2011/06/3.11.11-MFA-Letter-on-Accredited-Investor.pdf.

[6] In our view, the proposed rule would also comply with the SEC's obligations when conducting a rulemaking to consider costs and benefits of the rule, and would meet the requirements of Section 2(b) of the Securities Act of 1933, which requires the SEC to consider whether the action would promote efficiency, competition, and capital formation. For additional discussion of the benefits of the elimination of the ban on general solicitation for private funds, please refer to Rulemaking Petition from Richard H. Baker, President and CEO, MFA, to Elizabeth Murphy, Secretary, SEC (Jan. 9, 2012), available at: http://www.sec.gov/rules/petitions/2012/petn4-643.pdf.

I. Verification of Accredited Investors

We continue to recommend, however, that the SEC provide issuers with additional legal certainty when an investment amount is sufficiently high and the purchaser certifies that it is in fact an accredited investor. In general, an individual is an accredited investor if he or she has a net worth that exceeds $1,000,000, and an entity is an accredited investor if it has total assets that exceed $5,000,000. Accordingly, we respectfully urge the SEC to adopt a safe harbor in the final version of Rule 506(c) that would deem an issuer to have complied with the verification requirement if a purchaser, in addition to providing certifications that it is an accredited investor and has not obtained financing for the transaction, meets a certain minimum investment level that the SEC determines based on these thresholds.

In considering the appropriate minimum investment level, we have previously recommended a minimum investment level of 50% of the accredited investor net worth or total asset thresholds, currently $500,000 for an individual, and $2,500,000 for an entity. This recommendation is based on an analogous approach to investor qualification that the SEC has used for many years in the definition of "qualified client" in Rule 205-3 under the Investment Advisers Act of 1940.[7] Under this standard, an investor who has assets under management with an adviser that are at least half of the value of the net worth threshold is deemed to meet the qualification requirement. We believe a similar approach is appropriate for the verification of an accredited investor.

In the alternative, the SEC should adopt a safe harbor in Rule 506(c) where a purchaser certifies, as described above, that it is an accredited investor and did not obtain financing for the transaction, and invests some minimum amount up to the net worth and total asset thresholds in the definition of accredited investor. Any minimum investment amount included in a safe harbor should be adjusted proportionally in accordance with any future changes to the accredited investor net worth and total asset thresholds.

II. Guidance on Minimum Investment Amounts

If the SEC does not include a safe harbor for a minimum investment, we recommend that the Commission describe in the adopting release how an issuer should incorporate a purchaser's investment amount into its analysis of the facts and circumstances of a transaction. We appreciate that the proposing release indicates that an issuer conducting an offering with a high minimum investment may not need to take additional verification steps, other than to confirm that the investment is not being financed by the issuer or by a third party.[8] We note, however, that an issuer would not be able to determine independently whether an investment is financed by a third party; rather, an issuer could confirm that the issuer itself has not financed the transaction, and obtain a certification from the purchaser that it has not obtained financing for the transaction.[9] We believe that such a process, together with a sufficiently high investment minimum and a certification from the purchaser that it is an accredited investor, should fulfill the requirement that an issuer take reasonable steps to verify the status of the purchaser.

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[7] A "qualified client" is an investor whom the issuer reasonably believes has a net worth of more than $2,000,000, or an investor who has at least $1,000,000 under the management of the adviser.

[8] 77 Fed. Reg. at 54469.

[9] The SEC might also consider whether an investor could provide a certification that any financing obtained for a transaction was not used by the investor to meet the minimum investment amount.

III. Definition of Accredited Investor

We agree with the SEC's determination that the JOBS Act does not amend the definition of "accredited investor," and that the definition continues to include a person whom an issuer reasonably believes falls within one of the categories set out in the definition.[10] Accordingly, an issuer that takes reasonable steps to verify that an investor is an accredited investor, and reasonably believes that such an investor is an accredited investor, should be deemed to comply with the verification requirement.

Eliminating the "reasonable belief" standard in the definition of accredited investor would preclude issuers from relying on Rule 506(c). Under such an approach, an investor who provided an issuer with fraudulent documentation during the verification process could cause the issuer to violate Regulation D, despite the best efforts of the issuer to take steps to verify that the investor was an accredited investor. Issuers would not engage in general solicitation and Section 201 would fail in its intended purposes to modernize the securities laws.

IV. Existing Investors in Private Funds

We also recommend that the SEC confirm that private funds and other issuers with existing investors who are not accredited investors will be able to rely on new Rule 506(c) by complying with the applicable requirements with respect to future investments in the private fund.[11] This approach is consistent with the language and underlying policy of the JOBS Act. Section 201(a) instructs the SEC to eliminate the ban on general solicitation for offers and sales of securities made pursuant to Rule 506, provided that all purchasers of the securities are accredited investors. Accordingly, the requirement that all purchasers are accredited investors should apply only to future sales made pursuant to Rule 506(c), and should not require an issuer to either redeem or buy out existing investors, or incur the burdens of organizing an entirely new private fund.

Including a "grandfathering" provision for existing investors is also consistent with the goal of Section 201(a) to ensure that any investor who may have learned about the issuer through general solicitation or advertising is an accredited investor. Issuers that currently conduct offerings under Rule 506, such as private funds, are prohibited from engaging in general solicitation. As a result, existing investors have not been subject to any general solicitation activities, and should be able to maintain their investments in private funds that rely on Rule 506(c) in future offerings.

V. Proposed Changes to Form D

We support the proposal that an issuer indicate on Form D whether it is relying on Rule 506(b) or Rule 506(c). Such an indication, however, may be of limited use to the SEC in monitoring general solicitation by private funds. Given the uncertainty about what activities may be deemed a general solicitation, we expect that many private funds will indicate on Form D, based on the advice of outside counsel, that they are relying on Rule 506(c) even if they do not intend to engage in actual solicitation activities. Some fund managers, for example, may rely on Rule 506(c) in order to respond to media inquiries or correct inaccurate information about a private fund, which may or may

[10] Rule 501(a).

[11] We note that future investments by existing investors should not include capital calls or rights offerings.

not be deemed a general solicitation, depending on the facts and circumstances. Other fund managers may maintain their current practices (*i.e*., not engage in any activity that could be deemed general solicitation), but nevertheless comply with the requirements of Rule 506(c) (*i.e*., reasonable steps to verify and limiting sales to accredited investors) as a precaution to avoid any inadvertent violation of Rule 506. In some instances, a private fund may be able to rely on both Rule 506(b) and Rule 506(c).[12]

Some commenters have recommended that the SEC make additional changes to Form D, including a requirement that issuers file Form D prior to making any offers or sales using general solicitation. We support the Commission's decision not to include these changes in the rulemaking proposal and to limit its scope to the implementation of Section 201(a).[13] We nevertheless would point out that a requirement to file Form D prior to an offer or sale would create even greater uncertainty for an issuer in indicating whether it will rely on Rule 506(b) or Rule 506(c). At such an early point in the offering process, an issuer may not be certain of the offering methods that will be most effective or the type of potential investors.

For these reasons, we recommend that the SEC confirm that an issuer may conduct an offering that meets the requirements of either Rule 506(b) or Rule 506(c), as long as it has provided a good faith indication of its intent at the time it completes the check-box on Form D. In other words, an issuer should be permitted to rely on Rule 506(c) even if it has in good faith indicated on Form D that it intends to rely on Rule 506(b), and an issuer should be permitted to rely on Rule 506(b) even if it has in good faith indicated on Form D that it intends to rely on Rule 506(c).

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[12] Some funds may rely on Rule 506(b) because they intend to permit as investors certain "knowledgeable employees," as defined in Rule 3c-5 under the Investment Company Act. While knowledgeable employees may invest in funds that rely on Section 3(c)(7) of the Investment Company Act, they are not included within the definition of accredited investor. As a result, some knowledgeable employees may not qualify as accredited investors, which would lead to the anomalous result that a 3(c)(7) fund may need to prohibit otherwise eligible purchasers in order to rely on Rule 506(c). *See* our attached May 4 letter for additional discussion.

[13] We have not provided comments in response to these additional recommendations because they were not included in the proposal and are not under consideration to be included as part of any final rulemaking.

MFA appreciates the opportunity to provide comments to the Commission regarding implementation of the JOBS Act. If you have any questions about these comments, or if we can provide further information, please do not hesitate to contact Matthew Newell, Associate General Counsel, or the undersigned at (202) 730-2600.

Respectfully submitted,

/s/ Stuart J. Kaswell

Stuart J. Kaswell
Executive Vice President & Managing Director,
General Counsel

Cc: The Honorable Mary L. Schapiro
The Honorable Elisse B. Walter
The Honorable Luis A. Aguilar
The Honorable Troy A. Paredes
The Honorable Daniel M. Gallagher

Meredith Cross, Director, Division of Corporation Finance
Norman Champ, Director, Division of Investment Management

MANAGED FUNDS ASSOCIATION
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June 26, 2012

VIA EMAIL

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Request for Comments on Regulatory Initiatives Under the Jumpstart Our Business Startups Act

Dear Ms. Murphy:

Managed Funds Association ("MFA")[1] appreciates the opportunity to provide comments to the Securities and Exchange Commission (the "SEC" or "Commission") in advance of its regulatory implementation of the Jumpstart Our Business Startups Act (the "JOBS Act"). We are writing as a follow-up to our previous letter[2] to provide additional recommendations regarding the implementation of Section 201(a)(1).[3]

Section 201(a)(1) directs the SEC to include in its rule a requirement that an issuer take reasonable steps to verify that purchasers of securities offered and sold under revised Rule 506 are accredited investors. In our previous letter, we explained that hedge fund managers have long implemented procedures to ensure that funds meet the requirements in Section 3(c)(1) or Section 3(c)(7) of the Investment Company Act of 1940, which include investor qualification standards. In general, each potential hedge fund investor must complete a subscription document provided by the

[1] The Managed Funds Association (MFA) represents the global alternative investment industry and its investors by advocating for sound industry practices and public policies that foster efficient, transparent, and fair capital markets. MFA, based in Washington, DC, is an advocacy, education, and communications organization established to enable hedge fund and managed futures firms in the alternative investment industry to participate in public policy discourse, share best practices and learn from peers, and communicate the industry's contributions to the global economy. MFA members help pension plans, university endowments, charitable organizations, qualified individuals and other institutional investors to diversify their investments, manage risk, and generate attractive returns. MFA has cultivated a global membership and actively engages with regulators and policy makers in Asia, Europe, North and South America, and all other regions where MFA members are market participants.

[2] Letter from Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel, MFA, to Elizabeth Murphy, Secretary, SEC (May 4, 2012), available at: https://www.managedfunds.org/wp-content/uploads/2012/05/MFA_Comments_on_JOBSAct_05-04-2012.pdf.

[3] Section 201(a)(1) instructs the SEC to revise Rule 506 of Regulation D under the Securities Act of 1933 to eliminate the prohibition against general solicitation or general advertising for offers and sales of securities made pursuant to Rule 506, provided that all purchasers are accredited investors.

fund's manager that provides a detailed description of, among other things, the qualification standards that a purchaser must meet under the federal securities laws. These procedures have functioned effectively for private fund managers and investors, and we believe these methods would meet the standards under Regulation D and Section 201.

We nevertheless recognize that Section 201 does not specify the types of reasonable steps to verify investors that may be appropriate, and we understand the SEC is considering imposing additional requirements on issuers. If the SEC determines that issuers that rely on revised Rule 506 must take additional steps to verify investors, it is crucial that such steps can be effectuated by investors and issuers in a practical, efficient manner that avoids undermining the clear intent of the JOBS Act to modernize private offerings and enhance capital formation.

The primary method for verification should continue to be a certification by the investor, which should be supplemented by appropriate, additional evidence.

First, we suggest that the SEC look to its own rules that provide a straightforward approach to investor verification. Rule 205-3 under the Investment Advisers Act of 1940 defines a "qualified client" as an investor whom the issuer reasonably believes has a net worth of more than $2,000,000, or an investor who has at least $1,000,000 under the management of the adviser.[4] Under this standard, an investor who has assets under management with an adviser that are at least half of the value of the net worth threshold is deemed to meet the qualification requirement.

The SEC may wish to consider adopting an equivalent approach under revised Rule 506. An issuer should be deemed to have taken reasonable steps to verify that a purchaser is an accredited investor if the investor certifies that it qualifies as an accredited investor, and a natural person investor has at least $500,000 under management with the issuer, or an entity investor has at least $2,500,000 under management with the issuer.[5] In other words, an issuer should be permitted to treat as an accredited investor an investor who certifies to that effect and has the funds to invest at least 50% of the required net worth or total assets, as applicable, in the accredited investor standard.

Second, in the case of an investor who does not meet this minimum investment level, an issuer should be deemed to comply with Rule 506 if the investor submits a certification that it qualifies as an accredited investor, and also provides some type of additional third-party evidence. The SEC should publish a non-exclusive list of the types of additional evidence that an investor could provide for these purposes, which should include:

(i) Bank or brokerage statement(s) indicating that the investor has at least $1 million (for individuals) or $5 million (for entities) in assets;

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[4] In 2011, the SEC amended the definition of qualified client in Rule 205-3 by raising the required assets under management from $750,000 to $1 million, and increasing the required net worth threshold from $1.5 million to $2 million. The amendments maintained the existing ratio between the thresholds. Order Approving Adjustment for Inflation of the Dollar Amount Tests in Rule 205-3 under the Investment Advisers Act of 1940, Investment Advisers Act Release No. 3236 (July 12, 2011).

[5] If in the future the SEC reviews and adjusts upward the net worth threshold for an accredited investor, it should proportionately adjust the assets under management threshold.

(ii) Audited financial statements (if the investor is an entity);

(iii) A copy of the primary summary pages of the investor's most recent tax return that contain basic information and signatures, or a copy of the investor's W-2 indicating that the investor meets the minimum income level; or

(iv) A statement of an independent third-party professional (*e.g.*, banker, certified public accountant, lawyer, entity chief financial officer, etc.) that the professional believes, after due inquiry, that the investor meets the definition of accredited investor.[6]

The rule should make clear that the evidence need not be created for, nor specifically addressed to, the issuer or fund manager; for example, a recent bank statement or letter from a certified public accountant should be sufficient. The rule should also clearly indicate that the list is non-exclusive, and explain that an issuer may equally satisfy the verification requirement by obtaining one of the documents included in the list, or another type of similar third-party evidence. Requiring an issuer to obtain only certain materials would be unworkable in practice due to the wide range of investors that participate in private offerings, and the differences in their ability and willingness to provide certain types of information.

We believe the approach described above would best fulfill the verification requirement while achieving Congress's primary objective in removing the general solicitation and advertising restriction – to enhance capital formation, facilitate the flow of information in a manner consistent with investor protection, and increase transparency of issuers conducting private offerings, including private funds. MFA believes that such an approach would constitute "taking reasonable steps to verify that the purchasers of securities are accredited investors," as Section 201 of the JOBS Act requires. Such a proposal would avoid overly restrictive procedures that would have the effect of thwarting the purposes of Title II of the JOBS Act. Unduly restrictive procedures effectively would apply a strict liability standard to an issuer seeking to rely on Rule 506, which Title II clearly rejects. Moreover, we believe that if an investor provides reasonable evidence indicating that it is an accredited investor, an issuer should not be liable for an investor that makes false statements and seeks intentionally to evade the law. Imposing a rule that is unworkable for issuers conducting private offerings will prevent them from engaging in general solicitation and advertising, thereby defeating the clear intent of Congress and eliminating the substantial public policy benefits that will flow from Section 201.

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[6] The statement from the third-party professional must be based on its reasonable belief. It would generally not be possible for a third-party professional to certify that an investor qualifies as an accredited investor, and in particular that the investor has a minimum net worth.

MFA appreciates the opportunity to provide comments to the Commission regarding implementation of the JOBS Act. If you have any questions about these comments, or if we can provide further information, please do not hesitate to contact Matthew Newell, Associate General Counsel, or the undersigned at (202) 730-2600.

Respectfully submitted,

/s/ Stuart J. Kaswell

Stuart J. Kaswell
Executive Vice President & Managing Director,
General Counsel

Cc: The Honorable Mary L. Schapiro
The Honorable Elisse B. Walter
The Honorable Luis A. Aguilar
The Honorable Troy A. Paredes
The Honorable Daniel M. Gallagher

Meredith Cross, Director, Division of Corporation Finance
Eileen Rominger, Director, Division of Investment Management

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May 4, 2012

VIA EMAIL

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Request for Comments on Regulatory Initiatives Under the Jumpstart Our Business Startups Act

Dear Ms. Murphy:

Managed Funds Association ("MFA")[1] appreciates the opportunity to provide comments to the Securities and Exchange Commission (the "SEC" or "Commission") in advance of its regulatory implementation of the Jumpstart Our Business Startups Act (the "JOBS Act"). We applaud the underlying intent of the JOBS Act to improve access to capital and enhance economic growth by reducing unnecessary regulatory burdens. In particular, we strongly support the sections of the JOBS Act that directly affect managers of hedge funds and other private funds, and we are pleased to offer our preliminary views on implementation of these provisions.[2]

Title II – Access to Capital for Job Creators

Section 201(a)(1) of the JOBS Act instructs the SEC to revise Rule 506 of Regulation D under the Securities Act of 1933 (the "Securities Act") to eliminate the prohibition against general solicitation or general advertising for offers and sales of securities made pursuant to Rule 506, provided that all purchasers are accredited investors. An issuer relying on revised Rule 506 must take reasonable steps to verify that purchasers are accredited investors. In addition, Section 201(b) amends Section 4 of the Securities Act to provide that offers and sales exempt under revised Rule

[1] The Managed Funds Association (MFA) represents the global alternative investment industry and its investors by advocating for sound industry practices and public policies that foster efficient, transparent, and fair capital markets. MFA, based in Washington, DC, is an advocacy, education, and communications organization established to enable hedge fund and managed futures firms in the alternative investment industry to participate in public policy discourse, share best practices and learn from peers, and communicate the industry's contributions to the global economy. MFA members help pension plans, university endowments, charitable organizations, qualified individuals and other institutional investors to diversify their investments, manage risk, and generate attractive returns. MFA has cultivated a global membership and actively engages with regulators and policy makers in Asia, Europe, North and South America, and all other regions where MFA members are market participants.

[2] In conducting its rulemaking, the Commission should consider, pursuant to Section 2(b) of the Securities Act, whether its action will promote efficiency, competition, and capital formation.

506 shall not be deemed public offerings under the federal securities laws as a result of general advertising or solicitation.[3]

Importantly, Section 201(b) ensures that offers and sales by all types of issuers pursuant to revised Rule 506 will continue to be treated consistently. As a result, hedge funds and other private funds will continue to be able to conduct private offerings in reliance on revised Rule 506 in the same manner as other issuers, and such offerings will be non-public offerings for purposes of the Investment Company Act of 1940 (the "Investment Company Act").[4] This provision is consistent with long-standing interpretive positions of the Commission that ensure equivalent treatment across the federal securities laws.[5] By codifying these positions, Section 201(b) provides continuity and certainty to fund managers that have relied on this legal framework for decades.

We strongly support these reforms to Regulation D, and believe they will have salutary effects for investors, policy makers, regulators and the hedge fund industry.[6] In January 2012, MFA submitted a formal rulemaking petition to the SEC requesting that it eliminate the ban on general solicitation and advertising in Rule 506 for offerings by hedge funds.[7] In the petition, we explain that eliminating the ban would improve regulation of the industry, enhance economic growth, and fulfill the objectives of recent Executive Orders[8] by:

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[3] "Securities laws" are defined in Section 3(a)(47) of the Securities Exchange Act of 1934 (the "Exchange Act") as: the Securities Act, the Exchange Act, the Sarbanes-Oxley Act of 2002, the Trust Indenture Act of 1939, the Investment Company Act, the Investment Advisers Act of 1940 (the "Advisers Act"), and the Securities Investor Protection Act of 1970.

[4] A private fund is an issuer that would be an investment company, as defined in Section 3 of the Investment Company Act, but for Section 3(c)(1) or Section 3(c)(7). Advisers Act Section 202(a)(29).

[5] The Commission regards transactions that comply with Rule 506 of Regulation D as non-public offerings for purposes of Section 3(c)(1) of the Investment Company Act, and has interpreted the public offering limitation in Section 3(c)(7) in the same manner as the limitation in Section 3(c)(1). *See* Revision of Certain Exemptions From Registration for Transactions Involving Limited Offers and Sales, Securities Act Release No. 6389 at n. 33 (Mar. 8, 1982); Privately Offered Investment Companies, Investment Company Act Release No. 22597 at n. 5 (Apr. 3, 1997).

[6] As the SEC proceeds with implementation, we encourage the SEC and the Commodity Futures Trading Commission (the "CFTC") to coordinate so that rules regarding general solicitation activities that apply to private funds are consistent and further the policy goals of Section 201. For example, MFA intends to discuss with the CFTC its Rule 4.13(a)(3), which provides an exemption from registration as a commodity pool operator and includes limitations on marketing activities.

[7] Rulemaking Petition from Richard H. Baker, President and CEO, MFA, to Elizabeth Murphy, Secretary, SEC (Jan. 9, 2012), available at: http://www.sec.gov/rules/petitions/2012/petn4-643.pdf.

[8] In January 2011, the President issued Executive Order 13563, "Improving Regulation and Regulatory Review," which seeks to ensure that regulations protect public health, welfare, and safety while promoting economic growth, innovation, competitiveness, and job creation by using the best, most innovative, and least burdensome tools for achieving regulatory ends. In July 2011, the President issued Executive Order 13579, "Regulation and Independent Regulatory Agencies," extending Executive Order 13563 to independent regulatory agencies.

- Reducing legal uncertainty from the current regulation of private fund offerings conducted in reliance on Regulation D;

- Increasing transparency of the hedge fund industry in a manner consistent with the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") and recent regulatory initiatives;

- Facilitating capital formation and reducing administrative costs by allowing investors to more easily obtain information about private funds;

- Maintaining strong investor protections and ensuring that only sophisticated investors are able to purchase interests in private funds; and

- Reducing regulatory oversight costs and allowing the SEC staff to reallocate resources to other aspects of investor protection, including products offered and sold to retail investors.

We encourage you to review the rulemaking petition for a detailed discussion of the substantial improvements to the regulatory framework for hedge fund offerings that will follow from reforming Regulation D.

Most significantly, following implementation of Section 201, the regulatory framework for hedge funds will continue to ensure appropriate protections for investors. First, the activities of hedge fund managers in connection with offers or sales of securities will continue to be subject to the broad anti-fraud provisions of state and federal securities laws, including Section 17(a) of the Securities Act, and Section 10 of the Exchange Act and Rule 10b-5 thereunder. Hedge fund managers are also subject to the anti-fraud provisions applicable to all investment advisers in Section 206 of the Advisers Act. The Dodd-Frank Act has further strengthened oversight of hedge fund managers by requiring all managers with more than a *de minimis* level of assets under management to register with the SEC as investment advisers. As registered investment advisers, hedge fund managers are subject to a comprehensive regulatory framework under the Advisers Act, which includes periodic examinations and inspections by the SEC for compliance with the federal securities laws.

Second, and perhaps more importantly, only sophisticated investors may purchase interests in hedge funds, including those that in the future are offered and sold in reliance on revised Rule 506. Hedge funds that rely on Section 3(c)(7) of the Investment Company Act may only sell interests to "qualified purchasers," which include individuals with at least $5 million in investments, and institutions with at least $25 million in investments.[9] Hedge funds that rely on Section 3(c)(1) and conduct offerings pursuant to revised Rule 506 will only be permitted to sell interests to "accredited investors," and funds of this type managed by SEC-registered advisers generally only sell interests to "qualified clients," as defined in Rule 205-3 under the Advisers Act.

[9] Investment Company Act Section 2(a)(51).

In July 2011, pursuant to Section 418 of the Dodd-Frank Act, the SEC substantially raised the qualification thresholds for an individual in the definition of "qualified client."[10] The Dodd-Frank Act has also strengthened the "accredited investor" standard by excluding the value of a primary residence from an investor's net worth, instructing the Commission to increase the net worth threshold above the existing level of $1 million, and permitting the SEC to undertake a broad review of the definition of "accredited investor" for the protection of investors, in the public interest, and in light of the economy.[11]

MFA has consistently supported efforts to raise these qualification standards, which ensure that only sophisticated investors with the financial wherewithal to understand and evaluate the investments are able to purchase interests in private funds.[12] These sophisticated investors also typically perform extensive due diligence prior to investing with a particular manager, which includes reviewing and evaluating the substantial information about a fund and its manager contained in the fund's offering materials.

Accordingly, for many years the SEC staff has acknowledged that the ban on general solicitation is unnecessary for offers and sales made to "qualified purchasers" that are able to purchase interests in private funds that rely on Section 3(c)(7). Twenty years ago, in its 1992 report *Protecting Investors: A Half Century of Investment Company Regulation*, the Division of Investment Management's recommendation to Congress regarding the addition of Section 3(c)(7) to the Investment Company Act did not include a prohibition on 3(c)(7) funds engaging in public offerings. More recently, in its September 2003 report entitled *Implications of the Growth of Hedge Funds*, the SEC staff recommended that the Commission consider eliminating the general solicitation prohibition for 3(c)(7) funds, explaining that this change would not raise investor protection concerns.[13]

This long-standing staff position continues to be compelling with respect to not only 3(c)(7) funds, but also funds in which all purchasers meet the heightened qualification thresholds in the definition of "accredited investor." These investor restrictions ensure that only sophisticated institutions and individuals may purchase interests in these funds, which eliminates the risk that other

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[10] Order Approving Adjustment for Inflation of the Dollar Amount Tests in Rule 205-3 under the Investment Advisers Act of 1940, Investment Advisers Act Release No. 3236 (July 12, 2011) (adjusting the required assets under management from $750,000 to $1 million, and the required net worth from $1.5 million to $2 million). The SEC has also excluded the value of an individual's primary residence from the net worth calculation, and will adjust such amounts to account for inflation every five years. Investment Adviser Performance Compensation, Investment Advisers Act Release No. 3372 (Feb. 15, 2012).

[11] Section 413 of the Dodd-Frank Act.

[12] *See* Letter from Stuart J. Kaswell, Executive Vice President & Managing Director, General Counsel, MFA, to Elizabeth Murphy, Secretary, SEC (July 8, 2011), available at: http://www.managedfunds.org/wp-content/uploads/2011/09/MFA-Comments-on-Qualified-Client-Proposal.pdf; Letter from Richard H. Baker, President and CEO, MFA, to Elizabeth Murphy, Secretary, SEC (Mar. 11, 2011), available at: http://www.managedfunds.org/wp-content/uploads/2011/06/3.11.11-MFA-Letter-on-Accredited-Investor.pdf.

[13] Available at: http://www.sec.gov/news/studies/hedgefunds0903.pdf.

types of investors could be defrauded and lose money by investing in these funds as a result of a manager engaging in general solicitation or advertising.

Knowledgeable Employees

As described above, Section 201 of the JOBS Act is designed to permit general solicitation and advertising in connection with offers and sales under Rule 506 as long as all purchasers are sophisticated investors. In light of this policy objective, as part of its rulemaking the Commission should include in the definition of "accredited investor" an additional category of investor – a "knowledgeable employee" under the Investment Company Act – that Congress has determined possesses the requisite knowledge and sophistication to purchase interests in private funds.

In the National Securities Markets Improvement Act of 1996 ("NSMIA"),[14] Congress directed the SEC to adopt rules to permit the ownership of securities by knowledgeable employees of a 3(c)(1) fund or 3(c)(7) fund, or its affiliate.[15] In 1997, the SEC adopted Rule 3c-5 under the Investment Company Act to define the term "knowledgeable employee" to include two categories of employees of a private fund or its affiliated investment manager: (i) any person who is an "executive officer," director, trustee, general partner, advisory board member, or person serving in a similar capacity, and (ii) any employee who, in connection with his or her regular functions or duties, participates in the investment activities of the 3(c)(1) fund or 3(c)(7) fund, other private funds, or certain other investment companies.[16]

Pursuant to Rule 3c-5 and interpretive guidance issued by the SEC staff, many employees of hedge fund managers who are "knowledgeable employees" own interests in a 3(c)(1) or 3(c)(7) fund for which they perform investment functions. In the case of a 3(c)(7) fund, these employees are permitted to invest in the fund notwithstanding the wealth requirement in the definition of "qualified purchaser," which is substantially higher than the comparable requirement in the definition of accredited investor. Some of these knowledgeable employees, such as those who have been recently hired by a fund manager, do not qualify as accredited investors. In our view, it would be inconsistent to effectively prohibit these employees from investing in private funds as a result of the accredited investor standard, when Congress has explicitly determined that they may invest in private funds available only to investors that meet the higher "qualified purchaser" standard.

This long-standing policy of permitting knowledgeable employees of an investment manager to invest in a private fund is critical to meeting the demands of institutional investors, which seek to

[14] Pub. L. No. 104-290, 110 Stat. 3416 § 209(d)(3).

[15] A fund may rely on Section 3(c)(1) if its outstanding securities are beneficially owned by not more than 100 persons and it is not making and does not presently propose to make a public offering of its securities. A fund may rely on Section 3(c)(7) if its outstanding securities are owned exclusively by qualified purchasers, and it fund is not making and does not at that time propose to make a public offering of such securities.

[16] Rule 3c-5 effectively modifies the requirements imposed by Sections 3(c)(1) and 3(c)(7) by permitting a "knowledgeable employee" to acquire securities issued by a 3(c)(1) fund without being counted for purposes of the 100-person limit in Section 3(c)(1), and regardless of whether the knowledgeable employee is a qualified purchaser for purposes of Section 3(c)(7).

have their interests aligned with the interests of the fund's principals and the employees of the fund's manager. A primary method of achieving this alignment of interests is by permitting investment manager employees to make investments in funds they advise along with the investors. Our members generally have observed, over the past decade, an increasing number of institutional investors that look specifically to invest in funds in which the funds' principals and investment manager employees are significantly invested. In some cases, such institutional investors expect to receive investment terms that require a fund to provide notification if a certain amount of principal or employee investment is withdrawn from the fund. As a response, many of our members attempt to satisfy institutional investors by requiring investments by fund principals and investment manager employees as a means to encourage long-term risk-adjusted returns and to discourage undisclosed risk taking. It would be disruptive to private funds and their investors if a manager were no longer able to permit certain of its employees who participate in the investment activities of the fund to own interests in the fund.

We believe such "knowledgeable employees" of a private fund manager have an equivalent level of sophistication and financial wherewithal as accredited investors, and are therefore of the type that Congress intends to be eligible to purchase interests in offerings conducted pursuant to revised Rule 506. Accordingly, we recommend that as part of the implementation of Section 201, the SEC amend the definition of "accredited investor" to include those individuals who meet the definition of "knowledgeable employee" in Rule 3c-5 under the Investment Company Act.[17]

Reasonable Steps to Verify that Purchasers are Accredited Investors

Section 201(a)(1) directs the SEC to include in its rule a requirement that an issuer take reasonable steps to verify that purchasers of securities offered and sold under revised Rule 506 are accredited investors. We support this requirement and agree that it is important to ensure that only sophisticated investors are permitted to purchase interests in the types of offerings that will be conducted pursuant to revised Rule 506.

For many years, hedge fund managers have implemented procedures to ensure that funds meet the requirements in Section 3(c)(1) or Section 3(c)(7) of the Investment Company Act, which include investor qualification standards. As a result of these requirements, hedge fund managers have extensive experience, as compared to other types of issuers that may rely on Rule 506, assuring themselves that investors in private funds meet applicable qualification standards. In general, each potential hedge fund investor must complete a subscription document provided by the fund's manager that provides a detailed description of, among other things, the qualification standards that a purchaser must meet under the federal securities laws. In completing the subscription materials, each investor must identify which applicable qualification standard it meets. In addition to these procedures, many hedge funds managed by MFA members obtain further assurance of the qualification of their investors by virtue of minimum investment thresholds that meet or exceed the net worth requirement in the definition of accredited investor.

These procedures have functioned effectively for private fund managers and investors and have appropriately facilitated capital formation, and we believe similar methods would achieve the

[17] We note that under Section 413 of the Dodd-Frank Act, the Commission has authority at this time to amend the definition of "accredited investor," other than the net worth threshold.

comparable objectives of Section 201. We would be happy to further discuss these procedures with SEC staff as they proceed with implementation of Section 201.

Advisers Act Advertising Rules

In light of the elimination of the ban on general advertising and general solicitation for offers and sales made pursuant to revised Rule 506, it is also important to reconsider the advertising limitations created by the Advisers Act and rules promulgated thereunder.[18] In particular, MFA believes greater guidance and flexibility is necessary as to the types of information that registered or exempt private fund managers can provide in advertisements to existing or potential investors. Although the SEC and its staff have provided guidance on various advertising limitations in Section 206 and Rule 206(4)-1 of the Advisers Act,[19] uncertainty remains as to the scope and application of these limitations to private fund advisers. MFA's understanding is that the original intent of these restrictions was to address investor protection concerns related to adviser advertisements provided to *retail* investors. We fully support the need to protect investors and to ensure that the advertising materials that they receive are not deceptive or fraudulent. However, we believe that in the context of private fund advisers, which provide their advertisements solely to *sophisticated* investors, the current SEC no-action letter and legal guidance is counterproductive to this investor protection goal in that it makes it harder for private fund advisers to communicate effectively with their investors.

In the JOBS Act, by eliminating the general advertising and general solicitation restrictions, Congress expressed an intention to permit greater visibility of and transparency into entities, including private funds, which offer and sell securities pursuant to revised Rule 506.[20] It seems consistent with this policy of transparency (*i.e.*, allowing private funds to advertise broadly to the public), to also expand the information that private fund advisers can provide to their sophisticated investors. Moreover, MFA notes that potential investors desire to have, and frequently request, the types of information limited by these advertising restrictions and discussed in the SEC staff's guidance[21] because it ensures that they have a complete and robust view of any private fund manager

[18] Section 206(4) of the Advisers Act generally prohibits any registered or exempt investment adviser from engaging in any act, practice or course of business, which is fraudulent, deceptive or manipulative. Rule 206(4)-1 under the Advisers Act further defines such activities and limits advisers' ability to, among other things, publish, circulate or distribute advertising materials that refer to any testimonial or past specific recommendations of such adviser and places restrictions on the presentation of performance data in such advertising materials.

[19] *See e.g.*, Franklin Mgmt., Inc., SEC No-Action Letter (Dec. 10, 1998), which provides guidance related to the use of past specific recommendations in advertisements; Munder Capital Mgmt., SEC No-Action Letter (Aug. 28, 1997), which clarifies that investment adviser communications are advertisements if they are designed to maintain existing clients or solicit new clients; Clover Capital Mgmt., Inc., SEC No-Action Letter (Oct. 28, 1986), which provides specific guidance for advisers to follow related to advertisements that contain performance information.

[20] Reducing the restrictions on private fund managers' advertisements to sophisticated investors would be consistent with the policy objective of Section 201(a)(1) of the JOBS Act to permit general solicitation or general advertising for offers and sales pursuant to Rule 506, provided that all purchasers are accredited investors.

[21] We note that private fund managers provide such information only upon an unsolicited request from a potential investor. *See* Investment Counsel Association of America, Inc., SEC No-Action Letter (Mar. 1, 2004).

with which they have or expect to invest. Therefore, MFA believes it is consistent with Congressional intent and the protection of private fund investors to permit greater disclosure of information related to registered or exempt private fund managers in advertising materials; provided that, such information remains subject to the anti-fraud provisions otherwise applicable under the federal securities laws.[22] To assist the SEC with creating the necessary regulatory consistency, MFA will separately provide further recommendations for aligning the advertising rules in the Advisers Act with the JOBS Act and ensuring that private fund managers have greater clarity as to the types of information that they can provide to existing or potential investors.

Title V – Private Company Flexibility and Growth

Section 501 of the JOBS Act amends Section 12(g)(1)(A) of the Exchange Act by increasing the number of record holders of a class of equity security that will trigger registration, from 500 persons to: (i) 2,000 persons or (ii) 500 persons who are not accredited investors. MFA supports this amendment, which will help to resolve an unintended inconsistency in the regulation of private funds and mitigate an artificial burden to capital formation.

In 1996, Congress enacted Section 3(c)(7) to provide an additional method by which hedge funds and other private funds could be exempt from registration under the Investment Company Act. Prior to 1996, hedge funds could only rely on Section 3(c)(1), which exempts an issuer whose securities are beneficially owned by not more than 100 persons. Section 3(c)(7) takes a different approach than Section 3(c)(1) to the types of issuers that are not subject to the Investment Company Act. As described above, rather than limiting the number of investors in the fund, Section 3(c)(7) excludes any issuer whose outstanding securities are owned exclusively by persons who are "qualified purchasers." We believe that Congress's intent in adopting Section 3(c)(7), in addition to the then-existing Section 3(c)(1), was to permit a hedge fund relying on that Section to have an unlimited number of investors in the fund, as long as such investors were "qualified purchasers" or "knowledgeable employees."

Prior to the enactment of the JOBS Act, Section 12(g) of the Exchange Act frustrated this objective and impaired the capital raising activities of 3(c)(7) funds by requiring that a fund with more than 499 investors register its securities with the Commission. Registration of a class of equity security subjects domestic registrants to, among other things, the periodic reporting requirements of Section 13 of the Exchange Act, proxy requirements of Section 14, and insider reporting and short swing profit provisions of Section 16. These provisions are not appropriate to apply to hedge funds, and would provide little, if any, useful information to markets or regulators. Furthermore, as described above, investors in hedge funds are sophisticated individuals and institutions that often conduct extensive due diligence prior to investing, and also generally receive regular periodic reports about funds, including annual audited financial statements. Such investors generally do not require, nor would they expect, a hedge fund to provide the type of information about its operations that would be triggered by registration under the Exchange Act. As a result, hedge fund managers only permit up to 499 record holders of a class of fund interests.

[22] For example, the prohibitions on deceptive or fraudulent devices and schemes in Section 10(b) of the Exchange Act, Section 206 of the Advisers Act, and the related rules under each provision would continue to apply.

The increased shareholder threshold in Section 501 of the JOBS Act removes this artificial limitation and permits 3(c)(7) funds and other issuers to raise capital from more than 499 investors without triggering the registration requirement in Section 12(g). We believe this determination by Congress is appropriate as a result of the significant changes in the securities markets that have taken place since it enacted the original 499-person limitation in Section 12(g).

Section 504 of the JOBS Act directs the Commission to review whether additional tools are needed to enforce the anti-evasion provision in Rule 12g5-1 under the Exchange Act, and provide its findings to Congress. The anti-evasion provision applies to an issuer that knows or has reason to know that the form of holding securities of record is used primarily to circumvent the provisions of Section 12(g), and deems the beneficial owners of such securities to be the record owners thereof. MFA supports the objectives of the anti-evasion provision in Rule 12g5-1, and believes that the SEC should have the appropriate tools needed for enforcement of the provision. We note that hedge funds that rely on Section 3(c)(7) are already subject to a similar anti-evasion provision in Rule 2a51-3 under the Investment Company Act, which deems a company formed for the specific purpose of investing in a 3(c)(7) fund to be a qualified purchaser only if each beneficial owner of the company's securities is a qualified purchaser.

We would be pleased to respond to any questions related to the hedge fund industry that the Commission may have as it conducts its study pursuant to Section 504.

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MFA appreciates the opportunity to provide comments to the Commission regarding implementation of the JOBS Act. If you have any questions about these comments, or if we can provide further information, please do not hesitate to contact Matthew Newell, Associate General Counsel, or the undersigned at (202) 730-2600.

Respectfully submitted,

/s/ Stuart J. Kaswell

Stuart J. Kaswell
Executive Vice President & Managing Director,
General Counsel

Cc: The Honorable Mary L. Schapiro
The Honorable Elisse B. Walter
The Honorable Luis A. Aguilar
The Honorable Troy A. Paredes
The Honorable Daniel M. Gallagher

Meredith Cross, Director, Division of Corporation Finance
Eileen Rominger, Director, Division of Investment Management