



March 7, 2016

Brent J. Fields  
Secretary  
Securities & Exchange Commission  
100 F Street NE  
Washington, D.C. 20549-1090

**Re: File No. 4-692: SBIA Comments on the SEC Report on the Review of the Definition of Accredited Investor**

Dear Mr. Fields:

The Small Business Investor Alliance (“SBIA”) appreciates the opportunity to comment on the “Report on the Review of the Definition of ‘Accredited Investor’”<sup>1</sup> (“Report”) that was released on December 18, 2015 by the Securities & Exchange Commission (“SEC” or “Commission”).

SBIA is a national association that develops, supports, and advocates on behalf of policies that benefit investment funds that finance small and mid-size businesses in the lower middle market, as well as the investors that provide capital to these funds. Our membership consists of, traditional 3(c)(1) and 3(c)(7) private funds, funds and their investment advisers that have been licensed or are seeking to be licensed by the Small Business Administration (“SBA”) as small business investment companies (“SBICs”), funds registered as business development companies (“BDCs”) under the Investment Company Act of 1940, and the investors that invest in these funds, including banks, family offices and fund of funds.<sup>2</sup> Accredited investors are invested in many of our member funds.

**I. The Impact on SBIA Members Due to Recommendations on Adjusting the Accredited Investor Definition**

Our Members in making their offerings and sales of interests in their funds, overwhelmingly rely on Rule 506 of Regulation D for the exemption from registration under the Securities Act of 1933 and on section 3(c)(1) and/or 3(c)(7) of the Investment Advisers Act of 1940 for exemption from investment company registration requirements. Accordingly, these funds restrict their

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<sup>1</sup> U.S. Securities & Exchange Commission, *Report on the Review of the Definition of “Accredited Investor”*, December 18, 2015, available at: <http://www.sec.gov/corpfin/reportspubs/special-studies/review-definition-of-accredited-investor-12-18-2015.pdf>.

<sup>2</sup> SBIA currently has 165 individual fund/investment adviser members, and over 40 BDC members.

offerings to natural persons and entities that qualify as accredited investors, as defined under Rule 501 of Regulation D. Due to our Fund Members' reliance on Rule 506 for the offerings of their securities to investors, any change of the accredited investor definition to further limit its scope would have a significant negative effect on the ability of our members to raise capital for small business investments. We are particularly concerned with some of the Report's recommendations on the adjustment of the "accredited investor" financial thresholds, and the setting of new caps on the amount each investor can invest.

## **II. The Recommended Changes to the Income and Net Worth Thresholds in the Report, Will Reduce the Pool of Potential Investors in Small Business Funds & Fails to Make a Case For Why the Change is Needed**

In particular, the Report suggests the following changes which SBIA believes would significantly harm the pool of available capital for small business investment: (1) subjecting investors to new caps on investing to a certain percentage of income or net worth; (2) adding new inflation adjusted income and net worth thresholds that "update" the thresholds since 1982; and, (3) adding new inflation adjusted income and net worth thresholds on a *going forward* basis, grandfathering current accredited investors. While making these recommendations, the Report fails to provide any data or evidence that further restricting Americans from the ability to invest is needed. Further restrictions would not only be taking away the freedom of investment choice from more Americans, but would also have a significant impact on capital formation. These recommendations should not be adopted by the Commission, as they will greatly reduce the amount of capital available for investment and harm job creation. In effect they serve to only "protect" more Americans from the freedom of choosing their own investments and limit these investments to those who are already wealthy. Additionally, these changes are unnecessary because the financial thresholds were already significantly raised in 2011 (by excluding the primary residence from the calculation), and most importantly the SEC's has made the admission that there has been no demonstrated investor protection need to raise them again.

## **III. SBIA Supports The Report's Recommendations to Allow New Alternative Methods to Establish Financial Sophistication for Americans**

While we oppose the recommendations further restricting investor choice by raising the income and net worth thresholds, SBIA supports the other recommendations made in the Report, including (1) permitting spousal equivalents to pool their finances to achieve accredited investor status; (2) permitting certain entities such as Indian tribes, LLCs, labor unions, 529 Plans and others to qualify as accredited; (3) grandfathering existing accredited investors for future offerings from existing issuers; and, (4) expanding accredited investor status to those that can establish sophistication in other ways, including through an accredited investor education. These recommendations would not further hinder capital formation, small business investment, and

drive job creation. However a \$5 million threshold is very high and will severely limit investment by 529 Plans and other similar plans.

#### **IV. The Report Fails to Provide Sufficient Evidence of the Need for the Accredited Investor Financial Thresholds to be Raised**

The Report, while recommending potential changes, fails to provide any tangible evidence that the current financial thresholds under the Accredited Investor definition are insufficient to protect investors. Any increase in the financial thresholds under the accredited investor definition will further limit the number of people who can invest in small business funds and therefore reduce small business investment. Large funds are too large to invest efficiently in small businesses and investors in large funds tend to be institutions, not individuals. Smaller funds rely on individual investors and are appropriately sized to invest in small businesses. Increasing the thresholds through investment caps<sup>3</sup>, adjustment on current investors for inflation since 1982, or adjusting for the thresholds for inflation on a going forward basis, all possibilities recommended in the Report, will unfairly limit the ability of investors to access promising investment opportunities. In addition, these increases would also have particular detrimental effects for rural areas of the country that have difficulty in attracting large institutional investment capital, due to distance, differences in income and living costs, and make it difficult for small businesses and others to receive the capital they need for economic growth and job creation. As such, any changes to these thresholds must be approached with care, with strong evidence that investor protection is needed. The Report fails to present the evidence necessary to draw the conclusion that the thresholds must be changed to protect investors.

If the Commission plans to further restrict the freedom of individuals to invest, it should first establish that the current thresholds are a valid, not totally hypothetical and ideological, investor protection concern, which it has failed to do. In fact, the Report affirmatively concludes that there is no evidence of investor protection concern in regard to the current thresholds, stating that: “while the size of the accredited investor pool has increased significantly [since 1982], the staff is not aware of evidence suggesting that individuals qualifying as accredited investors under the current financial thresholds and participating in the Regulation D market require the protections of registration.”<sup>4</sup> This statement highlights that there is no evidence of investor harm suggesting a need to change the definition. In fact, nowhere in the Report does the SEC staff explain why inflation adjustments are needed, or why this larger pool of investors needs the “protection” of limiting their investment choices. The Report instead relies on letters from

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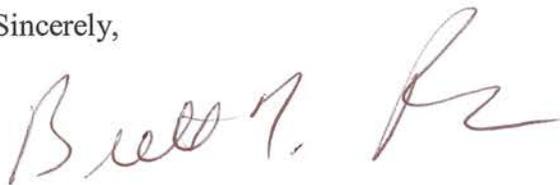
<sup>3</sup> While imposing caps on investments each individual can make based on net worth and income seems like a middle ground between raising the financial thresholds and leaving them as they are, the caps effectively impose an income and net worth requirement because most Regulation D offerings issued by private funds require a minimal investment amount of \$50,000. Setting a cap on investment would require those making this large an investment to have a higher net worth and/or annual income to meet the minimal investment amount, if based on percentage of income.

<sup>4</sup> Report at 89.

ideological special interest groups and others highlighting the “need” to raise these thresholds for the sake of raising them, rather than providing its own independent research from the Division of Economic and Risk Analysis (“DERA”).<sup>5</sup> A close review of some of the letters relied upon in the Report highlights that while they advocate for an increase in the threshold because of erosion by inflation, they provide no data supporting that investors are being harmed by the current definition, nor do they explain why the reduction in available capital for investment should be outweighed by their investor protection concerns.<sup>6</sup> Given the significant impact in changes to the definition, more research is needed before any action is taken by the Commission. Without independent research on the harm to investors presented by the current thresholds, and appropriate cost-benefit analysis against the impact of limiting investment opportunities and capital for economic growth, the SEC should move deliberately when considering the adoption of the Report’s recommendations.

SBIA is happy to provide continued feedback on this important issue to our membership. Please contact SBIA’s General Counsel, Christopher Hayes, at (██████████) or (██████████) if we can provide additional assistance on this issue.

Sincerely,



Brett Palmer  
President  
Small Business Investor Alliance

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<sup>5</sup> Report at 44-51.

<sup>6</sup> See Letter to the SEC from the American Federation of Labor and Congress of Industrial Organizations, *Comments on Amendments to Regulation D, Form D and Rule 156*, File No. S7-06-13, September 23, 2013, available at <http://www.aflcio.org/index.php/content/download/102841/2718291/AFL-CIO+comment+letter+on+File+No+S7-06-13.pdf>; Letter to the SEC from the Consumer Federation of America, *Comments on Amendments to Regulation D, Form D and Rule 156*, File No. S7-06-13, September 23, 2013, available at: <http://www.consumerfed.org/pdfs/CFA-Comment-on-GS-proposal-9-23-13.pdf>; Letter to the SEC from North American Securities Administrators Association (NASAA), *NASAA Comments in Response to Release Nos. 33-9416, 34-69960, IC-30595 (File No. S7-06-13), “Amendments to Regulation D, Form D and Rule 156 under the Securities Act”*, File No. S7-06-13, September 27, 2013, available at: <http://www.nasaa.org/wp-content/uploads/2011/07/NASAA-Comment-Letter-re-Form-D.pdf>.