



April 25, 2022

VIA ELECTRONIC SUBMISSION

Vanessa A. Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street NE
Washington, D.C. 20549-1090

Re: Private Fund Advisers; Documentation of Registered Investment Adviser Compliance Reviews (SEC Release No. IA-5955; File No. S7-03-22 (February 9, 2022)).

Dear Ms. Countryman:

The Los Angeles Venture Association (“LAVA”) appreciates the opportunity to submit this letter to the Securities and Exchange Commission (“SEC”) on the proposed rules (“Proposal”) regarding investment advisers to private funds.

Founded in 1984, LAVA represents venture/startup ecosystem in the greater Los Angeles metro area. The ecosystem is a mesh network of many diverse siloed communities, ranging from the tech scenes of silicon beach and playa vista to SOLA (South LA) and TenOneTen (Downtown LA); from the historic Pasadena area to the up-and-coming Riverside area innovation scene; and from the daring scientific discoveries in the many UC colleges and universities (Cal Poly SLO, LA, to Pomona) to the halcyon research institutes of Childrens’ Hospital, City of Hope, and Cedars.

Our emerging growth ecosystem produces innovations that save lives, products that change the world and, most importantly, a high percentage of above average wage paying jobs. When startups are funded in a neighborhood, they revitalize communities with small businesses, livable-wage jobs, and a thriving middle class. In the past few years, the venture ecosystem has finally experienced focus on diversity, equity and the genuine interest in not only making a profit and innovating, but also in making a difference.

Our community is on course to have the most women led funds, the most funds led by a person or people of color, and the most funds dedicated to ESG in the long 37-year history of LAVA. However, the SEC’s Proposal would create a major barrier to entry for many of these new funds and would significantly increase expenses and the need for more capital to perform the administrative tasks required to comply with many aspects of the Proposal. Substantive prohibitions would engender racial bias within an industry working to increase diversity, by imposing cost-prohibitive requirements for newly formed funds led by diverse emerging managers. The SEC promulgated an economic analysis the Proposal would have based on

historic information; however, the Commission did not consider the impact the Proposal would have on new entrants, women, and minority firms. Minority and women-owned funds historically receive less than 1% of all invested capital and will face even more significant barriers to entry and obstacles to growth if the Proposal is adopted.¹ In some ways, many of these funds are just as diverse and entrepreneurial as the companies in which they invest and enabled the record-breaking funding to diverse founders in the past 18-24 months. The Proposal would exacerbate the number of diverse founders that are unable to raise funds and fail as a result.

As detailed below, the extensive additional reporting requirements contemplated by the SEC will be enormously costly, potentially decreasing returns for the funds, their managers and their investors. Diverse emerging managers already often face challenges building their investor base and may lack the backoffice infrastructure needed to efficiently comply with the proposed reporting requirements, and thus risk being forced out of the market. Additionally, the Proposal would prohibit many funds from taking necessary risks by increasing liability that would not otherwise exist. The proposed prohibited-activities rules would also cause some funds to structure their fee and expense models in such a way that would raise investor's costs.

One of the primary issues with the Proposal is the SEC's plan to effectively eliminate the standard of care typically applicable to investment advisers, which at present holds a private fund sponsor liable for willful and egregious behavior. The gross negligence standard is critical to private equity, which as an asset class is fundamentally designed to encourage risk-taking by sponsors so that the investors might generate greater returns than they may experience with other classes. Investors will require managers to put in their own capital up to align interests and balance the risk/reward profile when many of the newer diverse fund managers lack the personal resources to do so. Additional standards of care beyond willful and egregious behaviors would quash their ability to take necessary, efficient, and mitigated risks particularly in diverse entrepreneurs, for the benefit of our Investors.

The Proposal would also have a drastic impact on our ability to choose a risk-adjusted return profile as part of a diversified portfolio. The Proposal looks to gray-up a settled area of law that is wholly unnecessary. Increasing liability for new managers will only cause irreparable harm to the already scarcity of emerging managers in the venture/startup space.

Furthermore, the requirement to obtain fund audits, prohibition of after-tax clawbacks, and prohibition of certain fees and expenses is signaling to all diverse emerging managers that the venture space is not an arena the SEC wants us to be able to fairly compete. The major, established venture firms, although not without drawbacks, will be able to abide by the Proposal, however, new formed micro fund firms will not be able to compete for talent, afford the

¹ See e.g. Securities and Exchange Commission Asset Management Advisory Committee - Subcommittee on Diversity and Inclusion - Recommendations for Consideration by the AMAC on July 7, 2021 *available at* <https://www.sec.gov/files/amac-recommendations-di-subcommittee-070721.pdf>

additional costs of unnecessary expenses, and create even more barriers for first time funds to be able to meaningfully fundraise.

As we previously stated, we write this letter to urge the SEC to truly considered the negative impact the Proposal will have on the firms and funds the Biden Administration wishes to help. The venture capital industry is going through an extremely healthy period of growth, where the power of venture capital managers no longer rests in the hands of a few, large, generalist funds, but is now being spread across an array of specialist funds. The industry continues to expand support for representation at both the entrepreneur and fund manager level.

We hope that this letter is helpful to the Commission in recognizing the limited resources and limited capacity of these emerging funds as it reconsiders this important Proposal. Please do not impede our industry's progress through unnecessary and frankly unlawful rulemaking. The policy rationale provided for many of the additional restraints on emerging funds is insignificant when compared to the detrimental impact the Proposal will have on diverse fund managers.

We thank you for allowing us the opportunity to comment on behalf of our members and our ecosystem, given that these are preliminary thoughts as we continue to digest the proposed rules, we will remain available to the SEC to discuss the impact the Proposal will have on our members.

Sincerely,

A handwritten signature in black ink, appearing to read 'Darren Eng', written in a cursive style.

Darren Eng
Executive Director
Los Angeles Venture Association