REISA
REAL ESTATE INVESTMENT SECURITIES ASSOCIATION

Real Estate Investment
Securities Association (REISA)

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March 11, 2011

Filed Via E-Mail

U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549
Attn: Ms. Elizabeth Murphy

Re: Section 413 of the Dodd-Frank Wall Street Reform and Consumer Protection Act; File No. S7-04-11

Dear Ms. Murphy:

On behalf of the Real Estate Investment Securities Association ("REISA"), this letter is submitted in response to the request of the staff of the Commission's Division of Corporation Finance (the "Staff") for comments on proposed rules related to the net worth standard for qualification as an "accredited investor" contained in Rule 501 of Regulation D under the Securities Act of 1933, as amended (the "1933 Act"). REISA is a trade organization serving the real estate securities industry including all professionals active in offering, managing and distributing non-traded REITs, real estate partnerships, tenant-in-common interests (TIC), Delaware statutory trust interests (DSTs), real estate income and development funds, oil and gas interests, natural resources and alternative energy investments.

REISA works to maintain the integrity and reputation of the industry by promoting the highest ethical standards to its members and provide education, networking opportunities and resources. REISA connects members directly to key industry experts through intimate forums providing timely trends and education; helping create a diversified portfolio for their clients. The association was founded in 2003 and has over 600 members who are key decision makers that represent over 20,000 professionals throughout the nation including:

- Sponsors and Managers of Real Estate Offerings
- Broker-Dealers
- Securities Licensed Registered Representatives
- Registered Investment Advisers (RIAs)
- Accountants
- Attorneys
- Mortgage brokers
- Institutional lenders
- Qualified intermediaries
- Real estate agents
- Real estate brokers

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REISA believes in the importance of protecting the investing public while balancing the need for businesses and sponsors of quality real estate investment products to be able to efficiently raise capital without an overly burdensome regulatory scheme.

As set forth below, REISA believes that the Staff's objectives of facilitating small business capital formation while protecting investors would best be served by:

(1) (a) Excluding both the value of the primary residence as well as all indebtedness secured by the primary residence from the calculation of net worth or

(b) in the alternative, excluding any debt that is non-recourse to the investor or his assets from the calculation of net worth regardless of whether such non-recourse debt is less than, equal to or in excess of the value of an investor's primary residence; and

(2) Including a grandfathering or transition provision for existing investments to allow investors, who previously qualified as accredited investors, to be able to continue to be treated as accredited investors so as to allow them to protect their current investments and investment positions.

Accredited Investor Net Worth Test

Section 413 of the Dodd-Frank Act modified the net worth test for a natural person accredited investor to $1 million, *excluding* the value of the individual's primary residence. The proposed amendments would add the phrase "calculated by subtracting from the estimated fair market value of the property the amount of debt secured by the property, up to the estimated fair market value of the property" after the word "residence."

REISA disagrees with the proposed amendment. First, the proposal is silent as to whether debt in excess of a residence's value is treated differently based upon whether such debt is recourse to the other assets of the investor. As the Staff noted in its proposal, the Staff adopts the conventional meaning of the term net worth – the difference between the assets and liabilities of a person. It would, therefore, be a contradiction to state that the debt in excess of the value of the primary residence should always be netted against the investor's other assets even if such assets would not be subject to a corresponding liability. REISA believes that the calculation of net worth for purposes of Section 413(a) of the Dodd-Frank Act should exclude both the value of, and all indebtedness secured by, the primary residence and in so doing, would more accurately reflect the practical economic impact of such indebtedness on an investor's true net worth.

Second, the proposed amendment's reliance on a determination of fair market value makes the calculation problematic and uncertain. Fair market value is both inherently subjective as well as subject to vagaries in the market that have no bearing on the sophistication of an investor or his

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ability to withstand the risks of an investment in a privately placed security. Thus, investors, broker-dealers, registered investment advisers and their associated persons would face substantial uncertainty when calculating net worth rather than a calculation that relies on certainty and objectivity. On the other hand, if the Staff were to exclude both the value of the primary residence as well as all indebtedness secured by the primary residence, investors and their advisors would have certainty regarding the calculation.

In response to the Staff's request for comment regarding treatment of debt secured by the primary residence used to buy securities, REISA agrees that it is unnecessary to include in the net worth calculation such debt secured by the primary residence which was used to buy securities. Tracking the source of the funds to make a purchase of securities would be difficult and overly burdensome for broker-dealers and registered investment advisers.

The Staff also asked whether a specific date for calculating net worth should be used – such as 30, 60 or 90 days prior to the date of sale. REISA believes that creating a specific date for the calculation of net worth would make the calculation of net worth unduly complex and place additional burdens on investors and their advisors without providing additional benefits or protections to investors.

Net Worth Definition "Grandfathering"

REISA also strongly believes that transition and grandfathering rules are appropriate in this context. In order to facilitate subsequent investments by an investor who previously qualified as an accredited investor but who was disqualified as such by the change in Section 413 of the Dodd-Frank Act, some kind of transition period and/or grandfathering rules should be implemented. Many of REISA members' investors have invested on average $360,000 in each investment program. Prohibiting such investors from making a subsequent investment or meeting an investment capital call because they have fallen out of the status of an accredited investor subsequent to their initial investment could cause investment significant losses and an enormous burden on these investors.

Between 2002 and 2008, approximately 1,325 offerings of Regulation D pooled real estate investments were made by sponsors. Those offerings represented at least 30,000 investors who invested total equity of almost $14 billion. The number of sponsors selling offerings in 2002 was 14 and peaked in 2006 at 71 sponsors. Given the current economic environment and the real estate market in general, many of the programs in which REISA members participated are encountering difficulties which could require various actions, including capital calls or modifications to the loan agreements and/or refinancings. If some of the investors in these offerings were to become non-accredited investors as a result of the implementation of the Dodd-Frank Act, those investors would be prohibited from participating in any of the actions that would be necessary to preserve their investment without dilution. In some cases, not participating in a

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capital call can trigger a forced buy out of the investor's position in a program, which may result in a large cash loss, as well as a taxable event. Sponsors would likely be unable to meet the disclosure requirements necessary to allow non-accredited investors to participate in any future investment decision (whether it was a capital call, loan modification or other exercise of rights necessary to preserve the investment). Prohibiting those investors from continued participation in their investment by prohibiting investing in future offerings of these programs would result in dilution or possible loss of their entire investment. If an investor was accredited at the time of the initial investment and made his investment decision based upon the information he received at the time of such investment, such investor should retain the right to protect that same investment notwithstanding the fact that he no longer fits within the definition of an accredited investor due to the changes made in the definition of accredited investor in the Dodd-Frank Act. To do otherwise would be unfair to investors whose significant investments may be diluted or lost or who may lose the ability to exercise certain rights related to such investment. REISA believes that these investors should be able to continue to be treated as accredited investors in the existing investments in which they are currently invested.

REISA also believes that existing investors should not be penalized solely because of the enactment of a new definition of accredited investor and that those investors who invested in a program as part of a 1031 exchange should be allowed to "roll over" their 1031 exchange money into a new investment structured as a 1031 exchange as an accredited investor so as to not incur a significant taxable event when the current 1031 program is over. If such investors were not able to do so, and were unable to find the same quality of real estate in which to invest, the tax consequences to them would be significant. However, REISA does not believe that investors should be treated as accredited investors for purposes of making any new investments unrelated to the investments in which they are currently invested, other than as described above.

NASAA "Invested Assets" Standard

In addition, REISA disagrees with the recommendation by the North American Securities Administrators Association to add additional qualifications to the accredited investor test for "invested assets" if the investor must qualify for this test under all circumstances. REISA would support the concept of three Accredited Investor tests in which at least one qualification must be met: (1) net worth, (2) income or (3) invested assets. REISA believes that an "invested assets" test is duplicative because the broker-dealer suitability analysis and the investment adviser's fiduciary duty standard already requires investors to be rejected from qualifying to invest in a private placement if they do not meet the diversification/concentration and portfolio allocation tests particular to that investor's individual situation.

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Contraction of Qualified Investors

Broker-dealers who generally have sold private placements have been significantly hurt by the economic downturn, as well as actions brought by investors either in arbitration actions or bankruptcy courts looking to reach commissions received by private placement broker dealers related to sponsor bankruptcies. A recent article in Investment News stated that almost 2,400 registered representatives have been displaced during the period beginning in March 2010 through February 2011 with the shuttering of approximately 13 independent broker-dealers, including five independent broker-dealers who each employed more than 200 registered representatives.[i] In addition, REISA is aware of at least eight other broker-dealers, primarily in the Regulation D private placement space, who have closed their operations over the past two years. The Dodd-Frank Act's revision to the accredited investor definition has reduced the size of the market for private placement securities by an estimated 20% to 50%. With the loss of significant numbers of broker-dealers in the private placement market, the contraction in the numbers of eligible investors, coupled with the increased costs of complying with regulatory burdens, there is significant pressure on the remaining broker-dealers in the private placement market. In addition, the decreasing availability of E&O insurance, increasing premiums and higher deductibles are putting pressure on small to mid-sized broker-dealer net capital minimums and causing them to evaluate whether or not they can continue to sell private placements. If the regulatory and insurance costs continue to increase, along with a shrinking pool of eligible investors, REISA is concerned that additional numbers of broker-dealers will exit the market and put small business capital formation at risk.

Conclusion

REISA believes that protecting investors is of paramount importance balanced with the needs of small businesses to engage in capital formation without an overly burdensome regulatory scheme. REISA appreciates the opportunity to comment on the proposed amendments to the accredited investor rules and looks forward to continuing the dialogue with respect to enhancing small business capital formation.

Sincerely,

Richard B. Chess

[i] "B-Ds down: Total reps displaced now approaching 2,400," Investment News, February 25, 2011.