

## VIA E-MAIL SUBMISSION

March 13, 2020

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

### **Re: RIN#3235-AM19, Amending the “Accredited Investor” Definition; File No. S7-25-19**

Dear Ms. Countryman,

The undersigned would like to sincerely thank the Commission for providing this precious opportunity to the public to comment on the newly proposed rule amending the current definition of “accredited investor”<sup>1</sup>. The undersigned really appreciates the way in which the SEC weighs every rulemaking decision based on diligent effort and rigorous analysis with a welcoming attitude. The undersigned believes the Commission’s collection of public comment is an extraordinary contribution to the nation’s democracy.

The undersigned is an international student who is pursuing a J.D. degree at Maurice A. Deane School of Law at Hofstra University. As an active participant currently enrolled in Securities Regulation class, the author has developed strong interest in relevant topics and discussions of legal issues in finance, securities, and banking fields, and would like to practice law of those areas addressed upon graduation. As a former intern of a law firm specialize in general business practice, the author assisted senior associates with multiple business issues. This practical experience also prepared the author for commenting on this proposal<sup>2</sup>.

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<sup>1</sup> The proposed rule can be found here: <https://www.sec.gov/rules/proposed/2019/33-10734.pdf>

<sup>2</sup> All views expressed herein are purely personal opinions of the undersigned. All comments made in this letter does not represent the opinion of the school or any organizations.

## **Summary of the Points**

The author agrees and supports the proposed changes, with a few recommendations stated in this letter. This letter is commenting on the first two categories<sup>3</sup> of natural persons newly added in the proposed rule. The newly proposed categories of entities will not be discussed in this letter.

In summary, these are the points that the author would like to make in the responses to the Commission's Request for Comments (#1, #9, #15, #17):

1. The author agrees with the Commission's idea to expand the definition of "accredited investor".
2. The professional certifications and designations should be maintained in good standing by their holders at the time of them being evaluating the qualification as accredited investors.
3. Knowledgeable employees of private funds should be added to the definition of accredited investor as proposed.
4. A knowledgeable employee's accredited investor status should be attributed to his or her spouse and/or dependents when making joint investments in private funds.
5. The component of the two categories are partially overlapped with each other, a combination of the two categories would reasonably solve such redundancy.

### **1. Expanding the Current Definition is Necessary.**

There are a few challenges in the current definitions of accredited investor. Current definition has very limited description of conditions a natural person should met as a qualified accredited investor.

In Rule 501 in Regulation D, a natural person as an accredited investors shall have "an individual net worth, or joint net worth with that person's spouse, exceeds \$1,000,000", or "an individual income in excess of \$200,000 in each of the two most recent years or joint income with that person's spouse in excess of \$300,000 in each of those years and has a reasonable expectation of reaching the same income level in the current year", and

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<sup>3</sup> The two categories refer to: (1) Persons who hold certain professional certifications and designations and other credentials showing their financial sophistication; (2) persons who are "knowledgeable employees" of a private fund and are investing in the private fund.

“directors, executive officers, and general partners of the issuer or of a general partner of the issuer.” Apparent enough to view, the only aspect of consideration is the individual wealth of the natural person. Realistically speaking, natural persons whose net worth or assets reached the requisite monetary threshold may not have the equally sufficient financial sophistication to make their investment decisions or participate in the current finance market with full awareness of the rules and potential risks. Thus, those natural persons shall not be qualified as accredited investors themselves. The author believes this is one of the concerns that the Commission currently have which promotes the proposed amendments to the current definition.

Having a broader and better scope of financial sophistication, the definition of accredited investor set forth in Section 2(a)(15)(ii) of the 1933 Act does contain languages describing a more comprehensive consideration of the qualified natural persons. It provides that the qualification should be granted to “any person who, on the basis of such factors as financial sophistication, net worth, knowledge, and experience in financial matters, or amount of assets under management qualifies as an accredited investor under rules”. However, there was no clear and explicit language setting a standard to interpret each “financial sophistication” factors set forth in this statute. A more concrete interpretation of each factors shall be further specified. For example, the undersigned believes it would be better to interpret the “knowledge” factor as: a systematic understanding of the basic rules and risks or general practice of financial activities in the current market. Such understanding or awareness could be gained from prior experiences or through the study of a particular exam designed for natural persons who are interested in stepping into the “world of investment”. The newly added two categories are fit for providing interpretations and guidelines to each factor set forth in the statute. This is one of the reasons the author supports the expansion of definition decision made by the Commission.

Lacking more concrete standards, those languages in the current definition to some extent are not clear and explicit enough. It may increase the difficulty of assessing qualifications of investors. Should any dispute arise from the granting of qualification, further interpretation of the statute is always needed. Such demand of explanation and interpretation will place more compliance burdens assessing natural persons. It is the author’s belief that the statutory factors shall be given more weight, with the assessment from multiple perspectives, the issuer shall be responsible for ensuring investors’ financial sophistication.

The Commission believes “wealth” in the current definition should not be the sole means of establishing financial sophistication; other factors should be included in the consideration to assess the qualification. By expanding the existing definition, the Commission intends to achieve these purposes: to expand the pool of investors eligible to participate in and provide capital to the Regulation D market; to avoid investment losses of those certification holders caused by not being recognized as accredited investors under current financial thresholds; to create a better alternative to assess investors’ need for protections of registration under the Act; and to reduce issuers’ compliance burden and simplify the current assessment procedure.

Besides the purposes and possible outcome listed above, another basis of the author's support to the proposed expansion of definition is the potential benefits to hedge funds. Pursuant to Regulation D, private funds can be offered and sold to "unlimited numbers of accredited investors". This provision makes accredited investor a crucial role in the capital raise of hedge fund. A larger pool of accredited investors would bring more capitals to the hedge funds, no doubt this is a direct positive impact of the expanded definition.

## **2. The Proposed Certifications, Designations and Credentials is an Appropriate Standard and They should be Maintained in Good Standing.**

In answering question #1 in the proposed release, the author believes professional certifications, designations and credentials is an appropriate standard; in addition, those credentials shall be maintained in good standing by their holder. While having a supportive opinion on the proposed "certification holder" standard, the author would like to kindly suggest the Commission to foresee some possible consequences if such category was added into current definition.

The study and preparation of certain exam would help a natural person to obtain a systematic understanding of a particular field. Applying this "common sense" to financial industry, the exams listed in the proposed release are feasible approaches for an individual to gain certain "keys" to the "world of investment". For instance, passing CFA would prove a natural person has the ability to conduct advanced financial analysis, securities analysis, and most importantly, the ability to start his or her career in finance industry. Such person, with profound understanding of most areas of finance, shall be assumed to have more "knowledge" and "financial sophistication" than average investor who is not a holder of any professional certificate. Comparing with other "random players" in this complex and risky game, the certification holders are more rational in decision making and more capable of coping with potential risks for the protection of themselves. Enlarging the pool of accredited investors by allowing those financially sophisticated persons in is a reasonable way to specify and particularize factors provided in Rule 215 with less effort.

As to the validity and general status of those certifications, designations, and credentials, the author would answer Question #9 in the proposed release with a solid "yes". Proving a natural person's financial sophistication is a process requiring consistency of the person's knowledge and understanding of the "rules of game". An outdated certification, even though still being a professional one, will not be an ideal and adequate indication of the person's current/then existing knowledge and understanding of securities transactions and general investment. Using an outdated certification or designation of the like at the time of being evaluated for the qualification as an accredited investor will likely result in loss of necessary protection from the Commission. A "consistent sophistication" shall be a requisite condition of a natural person to be an accredited investor to ensure that he/she

fully understand the risks and possible outcomes of the involvement in general/certain investment-making activity. Also, public availability of the authenticity and validity of the certifications should be maintained for issuers to assess qualifications of the holder.

It is respectfully submitted from the author to the Commission that with respect to the incentives of future “certification holders”, i.e., natural persons who plan to obtain professional certifications to gain a “ticket” to the “advanced player” playground in finance market. While the design of “certification holders” category is proper and appreciable, since the threshold of being an accredited investor is lowered by adopting such standard, the flood gate is open, and it would likely cause a substantial increase of numbers of natural persons who are eager for a try. There may be people who study for exams solely for the purpose of being accredited investors. A short-term “aggressive” study process would help to “boost the exam takers’ knowledge overnight”; however, after succeeding in gaining a “quick ticket”, would those individuals, who may have zero practical experiences in making investment, still be able to protect themselves waiving the shield of the Commission? With regard to this concern, the author agrees with the “minimum year of practice” suggested in Question #9.

### **3. Inclusion of Knowledgeable Employees is Beneficial to Private Funds.**

The following discussion is the undersigned’s response to Question #15 in the proposed release.

It is a fact that an individual who is a knowledgeable employee of private funds may not meet the financial threshold set forth in the current definition of accredited investors. Excluding those financially insufficient individuals as accredited investors would make them unable to participate in an offering of the private fund under Regulation D if the offering is limited to accredited investors. To avoid this, adding those individuals to the current definition would be an ideal solution.

Additionally, including knowledgeable employees in the definition of accredited investor would allow them to invest in the private fun without losing the fund’s accredited investor status when the funds with assets lesser than the current threshold of \$5 million. Such inclusion is an encouragement for those knowledgeable investors to invest in small funds while maintaining the eligibility of the fund’s qualification as accredited investors under Rule 501(a)(8).

#### **4. Knowledgeable Employee's Accredited Investor Status Can be Attributed to Spouses and Dependents When Making Joint Investments in Private Funds.**

Joint investment decisions were generally made by a group or a unit of individuals when they reached an agreement in making such investment. Abundant prior discussion and agreement should be presumed if such investment decision is made. In a familial context, the possibility of having conflicted investment decisions while taking actual steps to jointly invest in private funds is substantially low. As long as there is at least one accredited investor in the whole group or unit, sufficient financial sophistication of this particular joint investment should be assumed.

The joint investment in private funds should be view as a whole regardless of the total natural persons involved in the decision making. Therefore, the accredited investor status of a knowledgeable employee can be attributed to his/her spouse and dependents only when making joint investment, not a separate individual investment, in private funds. This is the author's view in responding question #17 in the proposed release.

#### **5. Certifications Accompanied with Minimum Practice Years/ Combination of the “Certification Holder” and “Knowledgeable Employee” Categories would Solve the Redundancy.**

With respect to the first two new categories of natural persons being discussed in this letter, the author agrees and appreciates most of the proposed amendments. However, there may be an existing redundancy in the design of the two categories. A “certification holder” who is outside the finance industry may not have enough practical experience to be able to qualify as an accredited investor, like what was discussed in Point 2 in this letter. Meanwhile, a “knowledgeable employee” in the second category may already holding certifications described in the first category

The author believes the expansion of the current definition of “accredited investor” is not a simple matter that could be solved ideally by making a single-dimension adjustment. Finance industry itself is a diverse field embracing participants with various backgrounds. Adjusting one factor would not be effective enough to solve an existing issue. A combination of theoretical study and practical experience in finance market could be a way to prove the sufficiency of natural persons' financial sophistication without setting the threshold too high or too low.

## **Summary**

Expanding current definition of “accredited investors” should be based on a careful analysis of the current definition’s effectiveness. Adding “certification holders” and “knowledgeable employees of private funds” to the definition would allow more natural persons with sufficient financial sophistication to the investment market, and such expansion would provide supplementary interpretation to the factors set forth in current Rule 215 definition.

However, the undersigned would recommend the Commission to conduct thorough analysis to foresee some of the possible outcomes if such expansion is enacted. Because rulemaking in this area is an important issue that would have an impact on the nation’s finance and economy. The Commission should take a cautious step in developing a balanced and reasonable designation of the categories of natural persons.

To assist the Commission with a more convenient and quick review of this comment letter, the author would like to attach a brief “Q&A” section. Here are the author’s brief responses to the questions requested for comments in the proposed release:

- **Question #1**

- Are professional certifications and designations or other credentials an appropriate standard for determining whether a natural person is an accredited investor?
  - ⇒ Yes.
  - ⇒ The author believes it is an appropriate standard if those “certifications” was maintained in good standing, accompanying a finance related practice experience of the investor, showing that the person is still an active participant in the current market with “fresh” sophistication to understand the rules and risks.
- Do the types of certifications and designations that the Commission is considering indicate that an investor has the requisite level of financial sophistication and abilities to render the protection of the Securities Act unnecessary?
  - ⇒ Yes.
  - ⇒ Meanwhile, careful assessment should be made to ensure the investor is capable of understanding the rules and risks. The person’s sophistication should be “fresh” enough to apply to the current investment market.

- **Question #9**

- Should the individual who obtain the designated professional credentials be required to maintain these certifications or designations in good standing in order to qualify as accredited investors, as proposed?
  - ⇒ Yes.

- ⇒ The validity and effectiveness of the certifications and designations is crucial to ensure that the investor has the requisite sophistication to comply with the current rules when engaging in financial activities and to protect himself/herself from potential risks.
- Should they also be required to practice for a minimum number of years?
  - ⇒ Yes.
  - ⇒ The undersigned believes that a combination of practice experience with the “certification” standard would be a more comprehensive approach to assess the investor’s financial sophistication.
  - ⇒ The undersigned agrees with the “minimum number of years of practice” requirement proposed in this question.

- **Question #15**

- Should knowledgeable employees of private funds be added to the definition of accredited investor as proposed?
  - ⇒ Yes.
  - ⇒ This would allow the financially sophisticated employees of private funds who did not meet the “wealth” threshold to involve in the market. It would be a beneficial to capital raise of hedge funds pursuant to Regulation D.

- **Question #17**

- Under the proposed definition of “accredited investor”, should a knowledgeable employee’s accredited investor status be attributed to his or her spouse and/or dependents when making joint investments in private funds?
  - ⇒ Yes, with conditions.
  - ⇒ The “accredited investor” status can be attributed to the knowledgeable employee’s spouse and/or dependents only when such investment decision was jointly made with agreement of all investors in this particular joint investment.

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