



MANAGED FUNDS
ASSOCIATION



March 13, 2020

Via Electronic Submission: rule-comments@sec.gov

Ms. Vanessa Countryman, Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

Re: Amending the Accredited Investor Definition

Dear Ms. Countryman:

Managed Funds Association¹ (“MFA”) and the Alternative Investment Management Association² (“AIMA”) (collectively, the “Associations”) appreciate the opportunity to provide comments in response to the proposed amendments to the definition of accredited investor (the “Proposal”).³ We commend the SEC for its efforts to update and modernize the definition to promote investment opportunities and facilitate capital formation while maintaining appropriate investor protections.

We support enhancing the definition of “accredited investor” and better aligning the various sophistication thresholds in the federal securities laws. In particular, we support the SEC’s determination in the Proposal to keep the financial thresholds as independent, objective qualification methods to ensure certainty for issuers, include knowledgeable employees of private fund advisers as accredited investors with

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 over time. MFA has cultivated a global membership and actively engages with regulators and policy makers in Asia, Europe, North and South America, and many other regions where MFA members are market participants.

² AIMA is the global representative of the alternative investment industry, with more than 2,000 corporate members in over 60 countries. AIMA’s fund manager members collectively manage more than \$2 trillion in assets. AIMA draws upon the expertise and diversity of its membership to provide leadership in industry initiatives such as advocacy, policy and regulatory engagement, educational programs and sound practice guides. AIMA works to raise media and public awareness of the value of the industry. AIMA set up the Alternative Credit Council (“ACC”) to help firms focused in the private credit and direct lending space. The ACC currently represents over 170 members that manage \$400 billion of private credit assets globally. AIMA is committed to developing skills and education standards and is a co-founder of the Chartered Alternative Investment Analyst designation (CAIA) – the first and only specialized educational standard for alternative investment specialists. AIMA is governed by its Council (Board of Directors).

³ SEC Release No. 33-10734 (Dec. 18, 2019), 85 F.R. 2574 (Jan. 15, 2020) (the “Release”).

respect to the funds managed by those advisers to better align the interests of investors and advisers, and expand the existing scope of entity types that meet financial thresholds that can qualify as accredited investors to promote consistency across different corporate forms. We provide additional discussion of each of these recommendations below.

I. Objective Standards Based on Net Worth and Income

The definition of “accredited investor” is an important standard for investors in private funds, and we commend the SEC for its Proposal to update and enhance the standard. Consistent with our prior letters on this subject, we support the SEC’s determination in the Proposal to maintain in the definition clear, objective standards based on the income and net worth of an investor.⁴ We agree with the statement in the Release that the current wealth-based criteria are useful for the identification of investors who do not require the protections afforded by registration, and that the use of financial thresholds as one method of qualifying as an accredited investor is appropriate.⁵

These objective standards are necessary to provide certainty to an issuer that an individual is an accredited investor, and consequently that an exempt offering will be conducted in compliance with Regulation D. In adopting Regulation D, the SEC carefully reviewed the existing regulatory framework and appropriately determined that issuers need to be able to rely on objective standards in conducting exempt offerings.⁶ As a result of these bright-line standards, Regulation D has been successful in promoting capital formation and protecting investors, and private issuers, including hedge funds, continue to depend on the legal certainty of quantitative, objective standards based on financial thresholds.

We also strongly support maintaining the existing aspects of the definition that provide that an accredited investor includes a person who meets one of the listed qualification methods, or who an issuer reasonably believes meets one of the qualification methods, at the time of the sale of the securities to the person.⁷ The reasonable belief standard provides issuers with substantial legal certainty when conducting an exempt offering, which is important to facilitate companies using Regulation D to raise capital.

With respect to the questions regarding potential increases to the income and net worth thresholds for individuals, we continue to support efforts to increase investor qualification standards for private fund investors over time, as appropriate, with a view to ensuring that only sophisticated investors with the financial wherewithal to understand and evaluate the investments meet the accredited investor definition, or other applicable sophisticated investor test under the federal securities laws.⁸ We have previously

⁴ Letter from Mark D. Epley, Executive Vice President and Managing Director, General Counsel, MFA, and Jiří Król, Deputy CEO, Global Head of Government Affairs, AIMA, to Vanessa Countryman, Secretary, SEC (Sept. 24, 2019), available at: <https://www.managedfunds.org/wp-content/uploads/2019/09/MFA-AIMA-Final-Letter-on-SEC-Concept-Release.pdf>.

⁵ 85 F.R. at 2593.

⁶ SEC Staff Report on the Review of the Definition of Accredited Investor (Dec. 18, 2015) (“SEC Staff Report”) at 18, available at: <https://www.sec.gov/corpfin/reportspubs/special-studies/review-definition-of-accredited-investor-12-18-2015.pdf>.

⁷ Rule 501(a) of Regulation D.

⁸ MFA supported the Commission’s proposal to amend the definition of accredited investor, pursuant to Section 413 of the Dodd-Frank Act, to exclude the value of a natural person’s primary residence for purposes of determining the net worth of a natural person. MFA also supported the Commission’s proposal in July 2011 to implement Section 418 of the Dodd-Frank Act by raising the qualification thresholds for an individual in the definition of “qualified client,” increasing the required assets under management from \$750,000 to \$1 million and the required net worth from \$1.5 million to \$2 million.

supported the recommendations noted in the SEC Concept Release on Harmonization of Securities Offering Exemptions⁹ from the SEC Staff Report to amend the income and net worth thresholds in the accredited investor definition to account for the effect of inflation, which would help to ensure that the thresholds have not been diluted over time. Similarly, we support indexing the thresholds for inflation. We also appreciate the discussion in the Release regarding the potential impact that higher thresholds could have on capital formation, and that the SEC will continue to consider the thresholds in connection with its quadrennial review of the accredited investor definition. In our view, these thresholds should remain independent qualification methods and should not include investment limitations or other qualitative conditions that would introduce uncertainty for an issuer seeking to confirm the status of an investor.

With respect to the proposed new categories of natural persons to qualify as accredited investors based on professional certifications and designations and other credentials, we encourage the SEC to provide a clear method for an issuer to verify such standards have been satisfied. For example, we agree with the statement in the Release recognizing that readily available information on whether an individual actively holds a particular certification or designation would be useful to an issuer, and the determination to include, as one of the criteria to be considered by the Commission in recognizing qualifying professional credentials, the public availability of information listing the individuals who hold the relevant certifications or designations.¹⁰

In addition, we recommend that in connection with any new categories of natural persons, the SEC confirm that any investors who qualify under such alternative standards are considered to be sophisticated investors and are not treated as retail investors under the federal securities laws. As the SEC has previously explained, the definition “encompass[es] those persons whose financial sophistication and ability to sustain the risk of loss of investment or fend for themselves render the protections of the Securities Act's registration process unnecessary.”¹¹ Accordingly, any new categories of natural persons should be treated the same as investors who meet other qualification methods in the definition of accredited investor, which together should not be subject to requirements applicable to retail investors.¹²

We also suggest that the SEC harmonize the existing sophisticated investor tests under the federal securities laws by including “qualified purchasers,” as defined in Section 2(a)(51) of the Investment Company Act of 1940, as amended (the “Investment Company Act”), as accredited investors. While we appreciate that the Commission has proposed amendments to the accredited investor definition to minimize the risk of a mismatch between the two definitions, we continue to believe that including all qualified purchasers within the definition of accredited investor would simplify compliance for private funds that seek investors who must meet both standards, without raising investor protection concerns.

⁹ SEC Release No. 34-86129 (June 18, 2019), 84 F.R. 30460 (June 26, 2019) (“Concept Release”).

¹⁰ 85 F.R. at 2582.

¹¹ Regulation D Revisions; Exemption for Certain Employee Benefit Plans, SEC Release No. 33-6683 (Jan. 16, 1987), 52 F.R. at 3017 (Jan. 30, 1987).

¹² See Letter from Carlotta D. King, Associate General Counsel, MFA, and Jiří Król, Deputy CEO, Global Head of Government Affairs, AIMA, to Vanessa Countryman, Secretary, SEC (Feb. 10, 2020), available at: <https://www.managedfunds.org/wp-content/uploads/2020/02/SEC-Proposed-Advertising-and-Solicitation-Rules-Final-MFA-and-AIMA-Letter.pdf> (recommending that in the proposed amendments to the advertising rule, Rule 206(4)-1 under the Investment Advisers Act of 1940, as amended, the Commission include “qualified clients” and “accredited investors” within the definition of “Non-Retail Person”).

II. Including Knowledgeable Employees as Accredited Investors

We strongly support the determination in the Proposal to permit “knowledgeable employees” of private fund managers, as defined in Rule 3c-5 under the Investment Company Act, to qualify as accredited investors for investments in private funds managed by their employers.¹³

Rule 3c-5 permits “knowledgeable employees” of a private fund to invest in the fund without being counted for purposes of the 100-investor limit in Section 3(c)(1) and without meeting the definition of “qualified purchaser” for a Section 3(c)(7) fund. The Rule is designed to permit investments by employees who have meaningful investing experience and sufficient access to information to make informed investment decisions about the fund. However, a knowledgeable employee may not meet the financial thresholds in the accredited investor definition and would, therefore, be excluded from participating in an offering of the fund if the offering is limited to accredited investors.

We agree with the statements in the Release that such knowledgeable employees, through their knowledge and active participation of the investment activities of the private fund, are likely to be financially sophisticated and capable of fending for themselves in evaluating investments in such private funds. We also agree that allowing these employees to invest in the funds for which they work will help to align their interests with those of unaffiliated investors in the fund.¹⁴ We urge the Commission to include knowledgeable employees in any final rulemaking that updates the definition of accredited investor.

III. Other Entity Types as Accredited Investors

We also support the proposed updates to the definition that would expand the types of entities that are able to qualify as accredited investors based on either their total assets or investments.

The Proposal would add limited liability companies to the types of entities that may qualify as accredited investors in Rule 501(a)(3), which currently includes any organization described in section 501(c)(3) of the Internal Revenue Code, corporation, Massachusetts or similar business trust, or partnership, not formed for the specific purpose of acquiring the securities offered, with total assets in excess of \$5 million. The Proposal would also add a new category for any entity owning investments, as defined in Rule 2a51-1(b) under the Investment Company Act, in excess of \$5 million that is not formed for the specific purpose of acquiring the securities offered.¹⁵

We believe these changes are appropriate and will provide objective, bright-line standards for issuers to determine whether certain types of entities qualify as accredited investors. Although the SEC staff has previously provided favorable guidance with respect to treatment of certain additional entity types as accredited investors, codifying the guidance to include limited liability companies in Rule 501(a)(3) and adding a new category providing that any entity meeting the requisite financial threshold can qualify as an accredited investor will reduce uncertainty and legal costs and promote more efficient private capital formation. We agree that a new corporate form could gain acceptance over time, similar to the emergence of limited liability companies, and that the proposed amendment would be effective in including these types of new entities, as well as existing entities such as Indian tribes and governmental bodies.

¹³ Proposed Rule 501(a)(11). We also note that a trust should qualify as an accredited investor if the grantor and trustee or person responsible for making the investment decision are knowledgeable employees. This accommodates common estate planning strategies for knowledgeable employees.

¹⁴ 85 F.R. 2585. *See also* SEC Staff Report.

¹⁵ Proposed Rule 501(a)(9).

In the Release, the SEC asks whether in addition to proposed Rule 501(a)(9) it should revise the definition of accredited investor by replacing the \$5 million assets test that currently applies to certain entities with a \$5 million investments test, and if so, whether it should grandfather existing investors that are currently accredited investors with respect to future offerings of their securities. We believe the \$5 million assets test has worked well and would recommend maintaining the test. If the SEC determines to replace the assets test with an investments test, we support a grandfathering provision such that an issuer's current accredited investors would continue to qualify as accredited investors in future offerings of the issuer's securities if they meet the current definition of accredited investor. We recommend that the SEC ensure that the grandfathering provision would apply to all securities of the particular issuer or its wholly-owned affiliates, and not only to the same securities currently owned by the investor. We believe permitting such an existing investor to make additional investments in any securities of the issuer is consistent with protecting from dilution in the future any investor who would no longer be an accredited investor because of the change to the definition.

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We appreciate the opportunity to provide these comments, and we look forward to continuing to provide what we hope will be useful and constructive comments on future Commission rulemakings. If you have any questions about these comments, or if we can provide further information, please do not hesitate to contact Ben Allensworth (ballensworth@managedfunds.org) or Matthew Newell (mnewell@managedfunds.org) at MFA, or Jennifer Wood (jwood@aima.org) at AIMA.

Respectfully submitted,

/s/ Mark D. Epley

Mark D. Epley
Executive Vice-President & Managing Director,
General Counsel
Managed Funds Association

/s/ Jiří Król

Jiří Król
Deputy CEO
Global Head of Government Affairs
Alternative Investment Management Association