



June 16, 2016

VIA EMAIL

Brent J. Fields
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: SEC Staff Report on the Review of the Definition of Accredited Investor; 4-692

Dear Mr. Fields:

Managed Funds Association (“MFA”)¹ appreciates the opportunity to provide comments to the Securities and Exchange Commission (the “SEC” or “Commission”) in response to the SEC Staff Report on the Review of the Definition of Accredited Investor (the “Report”). The definition of accredited investor is an important standard for investors in private funds, and we commend the SEC for undertaking a thorough review of potential methods to update and enhance the standard. Set out below are our views on the recommendations in the Report and other suggestions for the staff to consider.

Financial Thresholds to Qualify as an Accredited Investor

As a threshold matter, MFA believes it is essential that the definition of accredited investor continue to maintain clear, objective standards based on the income and net worth of an investor. These objective standards are necessary to provide certainty to an issuer that an individual is an accredited investor, and consequently that a private offering will be conducted in compliance with Regulation D. As described in the Report, Regulation D and its predecessor rules were originally adopted in response to widespread uncertainty among issuers seeking to conduct private offerings in accordance with the qualitative requirements of then-Section 4(2) of the Securities Act.² 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

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. 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 See Report at 10-16.

in conducting private offerings.³ 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 believe this approach has worked well over many years, and we strongly encourage the Commission to maintain standards based exclusively on net worth and income, notwithstanding any other changes to the definition.

We also strongly support the existing aspects of the definition 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.⁴ Under these standards, issuers are able to determine that a person is an accredited investor at the time of investment in a private offering, and are provided with additional legal certainty in their reasonable belief that a person is an accredited investor. We recommend that the SEC maintain these well-established standards in any updated definition of accredited investor.

With respect to the recommended increases to the income and net worth thresholds for individuals, MFA continues to support efforts to increase investor qualification standards for private fund investors over time, which ensure that only sophisticated investors with the financial wherewithal to understand and evaluate the investments are able to purchase interests in private funds.⁵ Investors in hedge funds generally must meet separate, additional qualification standards under the federal securities laws. Hedge funds that rely on Section 3(c)(7) of the Investment Company Act of 1940 (the “Investment Company Act”) may only sell interests to “qualified purchasers,” which include individuals with at least \$5 million in investments, and institutions with at least \$25 million in investments. Hedge funds that rely on Section 3(c)(1) generally only sell interests to accredited investors, and funds of this type managed by SEC-registered investment advisers generally only sell interests to “qualified clients,” as defined in Rule 205-3 under the Investment Advisers Act of 1940 (the “Advisers Act”).

Accordingly, we support the recommendations in the Report to amend the income and net worth thresholds to account for the effect of inflation, which would help to ensure that the thresholds have not been diluted over time.⁶ Similarly, we support indexing the thresholds for

³ Report at 18 (“Regulation D established bright-line tests for individuals to qualify as accredited investors based on their income or net worth.”)

⁴ Rule 501(a) of Regulation D.

⁵ 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. Available at: <http://www.managedfunds.org/wp-content/uploads/2011/06/3.11.11-MFA-Letter-on-Accredited-Investor.pdf>.

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. Available at: <http://www.managedfunds.org/wp-content/uploads/2011/09/MFA-Comments-on-Qualified-Client-Proposal.pdf>.

⁶ The Report describes two potential indices for calculating inflation adjustments, the Consumer Price Index (“CPI”) and the Personal Consumption Expenditures Chain-Type Price Index (“PCE”). We would recommend

inflation. Importantly, these thresholds should remain independent qualification methods under the definition of accredited investor, and should not include investment limitations or other qualitative conditions that would introduce uncertainty for an issuer confirming the status of an investor.

The Report recommends that following any increase in financial thresholds, 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. Under the recommendation, such a grandfathering provision would apply to future investments in a particular issuer, and not to future investments in affiliates of the issuer. We support this recommendation and agree that such a grandfathering provision would protect from investment dilution any person who would no longer be an accredited investor because of changes to the definition. We recommend that the SEC clarify 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 the investor from dilution in the future.

Additional Comments

If the SEC proceeds with increasing the financial thresholds, we agree that it would be appropriate to consider other changes to ensure that the accredited investor definition continues to include sophisticated individuals who have the ability to evaluate potential investments in private offerings. We strongly support the staff recommendation 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 of their employers. We agree with the conclusions in the Report that such knowledgeable employees have meaningful investing experience and sufficient access to information necessary to make informed investment decisions about the private fund's offerings. In addition, investments by knowledgeable employees are beneficial for private fund investors in that they further align investor interests with those of the fund manager.

Similarly, we recommend that the SEC further 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, as accredited investors, and by amending the definition of "qualified client" under the Advisers Act to include accredited investors. These changes would simplify the existing mismatch in standards for private fund investors without raising investor protection concerns. In particular, these changes would maintain existing financial thresholds and continue to ensure that only sophisticated investors are able to invest in private funds, as qualified purchasers include individuals with at least \$5 million in investments, and institutions with at least \$25 million in investments, and qualified clients are persons who

the method based on the PCE because it would provide consistency with the PCE method of inflation adjustment used in the definition of qualified client in Rule 205-3 under the Advisers Act.

have at least \$1,000,000 under the management of the investment adviser or have a net worth of more than \$2 million.⁷

The Report also has a recommendation to include, in addition to higher financial thresholds, a separate method to qualify as an accredited investor under the existing financial thresholds but also subject to investment limitations, such as 10% of prior year income or 10% of net worth, per issuer, in any 12-month period. If the SEC adopts such a qualification method, it should affirm that, consistent with the current definition of accredited investor, issuers will be able to determine that a person is an accredited investor at the time of investment and upon a reasonable belief of the person's qualification as an accredited investor.

Regarding other types of qualification methods, we agree that the SEC should consider whether individuals with certain professional credentials should qualify as accredited investors. For example, we recommend that the SEC consider including in the definition of accredited investor individuals who are certified public accountants or chartered financial analysts, and individuals who have received an MBA from an accredited educational institution. As noted in the Report, the CPA Exam includes a section that tests for knowledge of corporate governance, economics and finance, and a CFA must complete three CFA Institute administered examinations and have four years of relevant professional work experience. In addition, individuals who have received an MBA from an accredited institution have completed programs that provide them with a level of financial and business sophistication that should qualify them as accredited investors.

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MFA appreciates the opportunity to provide comments to the Commission regarding the Report and the definition of accredited investor. If you have any questions about these comments, or if we can provide further information, please do not hesitate to contact Matthew Newell, Associate General Counsel, or the undersigned at (202) 730-2600.

Respectfully submitted,

/s/ Stuart J. Kaswell

Stuart J. Kaswell
Executive Vice President & Managing Director,
General Counsel

⁷ The increased thresholds for the definition of accredited investor would be comparable to the existing thresholds for the definition of qualified client.