

June 1, 2020

Via Electronic Submission (rule-comments@sec.gov)

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

Re: Proposed Rule, Facilitating Capital Formation and Expanding Investment Opportunities by Improving Access to Capital in Private Markets, SEC Rel. No. 33-10763; File No. S7-05-20

Dear Ms. Countryman:

The Investment Adviser Association (“IAA”)¹ appreciates the opportunity to comment on the Commission’s proposal to amend rules governing the exempt offering process.² The Exempt Offering Proposal is the Commission’s third release in the past year focused on improving the exempt offering framework under the Securities Act of 1933 (“Securities Act”).³ The Concept Release sought input on ways to improve access to capital for a variety of issuers and access to investment opportunities for investors while maintaining investor protections, and the Accredited Investor Proposal proposed amendments to the definitions of “accredited investor” and “qualified institutional buyer” (“QIB”) under Securities Act rules. We support the Commission’s efforts to improve the exempt offering framework and offer some suggestions to assist in these efforts.

¹ The IAA is the largest organization dedicated to advancing the interests of investment advisers registered with the Securities and Exchange Commission (“SEC” or “Commission”). For more than 80 years, the IAA has been advocating for advisers before Congress and U.S. and global regulators, promoting best practices and providing education and resources to empower advisers to effectively serve their clients, the capital markets, and the U.S. economy. The IAA’s member firms manage more than \$25 trillion in assets for a wide variety of individual and institutional clients, including pension plans, trusts, mutual funds, private funds, endowments, foundations, and corporations. For more information, please visit www.investmentadviser.org.

² *Proposing Rule, Facilitating Capital Formation and Expanding Investment Opportunities by Improving Access to Capital in Private Markets*, SEC Rel. No. 33-10763 (Mar. 4, 2020), 85 FR 17956 (Mar. 31, 2020) (“Exempt Offering Proposal” or “Proposal”), available at <https://www.govinfo.gov/content/pkg/FR-2020-03-31/pdf/2020-04799.pdf>.

³ See *Concept Release on Harmonization of Securities Offering Exemptions*, SEC Rel. No. 34-86129 (June 18, 2019), 84 FR 30460 (June 26, 2019) (“Concept Release”), available at <https://www.govinfo.gov/content/pkg/FR-2019-06-26/pdf/2019-13255.pdf> and *Amending the “Accredited Investor” Definition*, SEC Rel. No. 33-10734 (Dec. 18, 2019), 85 FR 2574 (Jan. 15, 2020) (“Accredited Investor Proposal”) (proposing to include new categories of natural persons and institutions as accredited investors and qualified institutional buyers), available at <https://www.sec.gov/rules/proposed/2019/33-10734.pdf>.

I. Background and Summary of Recommendations

The ability of investors to access the capital markets is of critical importance to IAA members that act as fiduciaries for both institutional and individual clients. The IAA strongly supports improved access to these markets consistent with effective investor protection. In our responses to the Concept Release and the Accredited Investor Proposal, we recommended that the Commission adopt tailored amendments to the definitions of accredited investor and QIB that would improve access to private markets for clients of SEC-registered investment advisers.⁴ We urge the Commission to move forward with the Accredited Investor Proposal and in that context to adopt the IAA’s recommended changes to the accredited investor and QIB definitions.⁵ We also commented on the scope of “general solicitation” and “general advertising” in Regulation D under the Securities Act, and we reiterate and expand upon those comments below.

With regard to the current Exempt Offering Proposal, our comments are limited to the proposed verification of accredited investor status, the proposed “demo days” exemption, and the proposal related to testing the waters. We make the following recommendations:

- A. *Rule 506(c) Amendment – Verification of Accredited Investor Status.* We support and recommend that the Commission adopt its proposed amendment to Rule 506(c) under the Securities Act to add a new item to the non-exclusive list for issuer verification of accredited investor status. The new item would allow an issuer to treat as verified on an ongoing basis an investor for which the issuer previously took reasonable verification steps, under certain conditions. We also support the Commission’s proposal to reaffirm and update Commission guidance on what may be considered “reasonable steps” to verify an accredited investor’s status.
- B. *General Solicitation and General Advertising Prohibitions and Proposed Rule 148.* We appreciate the Commission’s efforts to provide an exemption from general solicitation and general advertising for certain “demo day” communications, but urge the Commission to clarify more broadly that communications not intended for public consumption do not constitute “general

⁴ The IAA’s comment letter on the Concept Release (“Concept Release Letter”) is available [here](#). The IAA’s comment letter on the Accredited Investor Proposal (“Accredited Investor Letter”) is available [here](#).

⁵ We recommended in our Accredited Investor Letter that the Commission amend the accredited investor definition in Rule 501 under Regulation D to include: (i) the discretionary clients of SEC-registered investment advisers; (ii) “qualified purchasers,” as defined in Section 2(a)(51) of the Investment Company Act of 1940 (“Investment Company Act”); (iii) “qualified clients,” as defined in Rule 205-3 under the Advisers Act; (iv) Investment Company Act Section 3(c)(7) qualified purchaser funds; and (v) SEC-registered advisers’ knowledgeable personnel investing on their own behalf. We also recommended that the Commission amend the QIB definition in Securities Act Rule 144A to expand opportunities for (i) discretionary separate account clients of SEC-registered investment advisers and (ii) families of private funds and other funds managed by SEC-registered investment advisers to participate in Rule 144A offerings.

solicitation” or “general advertising.” At a minimum, we recommend the proposed exemption under Rule 148 be broadened to include communications by sponsors of private funds that sponsor “demo days” and similar events.

- C. *Proposed Rule 241 – Solicitations of Interest.* We support the new exemption for testing-the-waters communications in proposed Rule 241. In response to the Commission’s request for comment, we support the proposal that the exemption not be limited to materials directed to institutional accredited investors (“IAIs”)⁶ and QIBs.

We discuss our recommendations below.

II. Recommendations

A. The Commission Should Adopt Proposed Amendments to Rule 506(c) and Further Streamline the Accredited Investor Verification Process

As a result of the JOBS Act, the Commission adopted paragraph (c) of Rule 506 under the Securities Act to permit general solicitation or advertising in offerings in which all purchasers are accredited investors, the issuer takes reasonable steps to verify that the purchasers are accredited investors, and certain other conditions in Regulation D are satisfied.⁷ Rule 506(c) provides a principles-based method for verification of accredited investor status, which requires an objective determination by the issuer (or those acting on its behalf) as to whether the steps taken are “reasonable” in the context of the particular facts and circumstances of each purchaser and transaction.⁸ Rule 506(c) also includes a non-exclusive list of verification methods that issuers may – but are not required – to use when seeking to satisfy the verification requirement with respect to natural person purchasers.⁹ The Commission recognizes, however, and we agree, that the prominent description of non-exclusive verification methods in the rule may be creating an incorrect impression that issuers (or those acting on their behalf) are permitted to rely only on the non-exclusive list rather than relying on the principles-based reasonable steps alternative.¹⁰

To address this confusion, the Commission proposes to add an additional non-exclusive optional method of verifying that a natural person who purchases securities in a Rule 501(c) offering is an accredited investor. The proposed additional method would allow issuers that have

⁶ See Rule 501(a)(1), (2), (3), (7) and (8) for a list of entities that are considered IAIs.

⁷ See Rule 501(c).

⁸ See Proposal at 17980.

⁹ See *id.*

¹⁰ See *id.*

previously verified accredited investor status for a natural person investor to obtain a written representation of accredited investor status from that investor at the time of sale, as long as the issuer is not aware of information to the contrary.¹¹ We support this rule amendment. We agree with the Commission that it would reduce the cost and burden on issuers to verify the investor's status where the investor may invest multiple times over time.¹² We also agree that privacy concerns of investors would be addressed by this approach because investors would no longer need to be providing sensitive financial information to an issuer repeatedly upon subsequent investments.¹³

The Commission requests comment on whether there are other verification methods that it should include in the rule's non-exclusive list.¹⁴ While we are not recommending any additional specific verification method(s), we believe the Commission should include a statement or note in the adopting release that would provide clearer assurances to issuers that they may rely on the principles-based reasonable steps approach. In this regard, it would be helpful for the Commission to confirm that it could be reasonable under the facts and circumstances for issuers to contract with a third party to conduct the required verification, although the ultimate obligation to verify status would remain with the issuer.

The Commission also asks if there are additional reasonable verification methods it should include for the new categories of natural person and IAIs in the Accredited Investor Proposal.¹⁵ We believe that the Commission should ensure that the verification methods in Rule 506(c) are able to clearly accommodate any modifications to the accredited investor definition.

B. The Commission Should Clarify that Communications Not Intended for Public Consumption Do Not Violate the “General Solicitation” or “General Advertising” Prohibition under Regulation D and Should Broaden Proposed Rule 148 for “Demo Days” to Include Similar Events Sponsored by SEC-Registered Investment Adviser Sponsors of Private Funds

In general, issuers of a non-public offering may not rely on an exemption from registration of their offering if they engage in “general solicitation” or “general advertising.” Rule 502(c) under Regulation D provides examples of these terms – including advertisements published in newspapers and magazines, communications broadcast over television and radio, and seminars where attendees have been invited by any “general solicitation” or “general

¹¹ Proposed Rule 506(c)(2)(ii)(E).

¹² Proposal at 17980.

¹³ *Id.*

¹⁴ Proposal at 17981 (Question 38).

¹⁵ Proposal at 17981-82 (Question 39).

advertising.” In our Concept Release Letter, we recommended that the Commission provide more clarity and specificity around these terms and also that it confirm that limited communications designed for consumption by a non-public audience (such as institutional publications or institutionally-focused consultant databases), or participation in a “demo day” or similar event, would not be considered “general solicitation” or “general advertising.” We reiterate that recommendation here.

We appreciate that the Commission has proposed new Rule 148, which provides a narrow exemption from the definition of “general solicitation” or “general advertising” for certain issuer communications at a “demo day” or similar event. Under the proposed rule, an issuer would not be deemed to have engaged in “general solicitation” or “general advertising” if the communications are made in connection with a seminar or meeting “by a college, university, or other institution of higher education, local government, nonprofit organization, or angel investor group, incubator, or accelerator sponsoring the seminar or meeting.” The issuer would need to meet certain other conditions as well.¹⁶ While the proposed rule is a step in the right direction, we believe it will be of limited utility because it is so narrow. The Commission also seeks comment on whether it should provide a definition of “general solicitation” and “general advertising” and/or eliminate all prohibitions on “general solicitation” and “general advertising” and focus on investor protections at the time of sale rather than at the time of offer.

In our view, a better approach to achieving the Commission’s goal of allowing issuers to present their businesses to targeted groups of sophisticated potential investors would be to provide clarification around what constitutes (or does not constitute) “general solicitation” and “general advertising.” We believe that issuer communications that are not intended to result in a sale to unqualified investors and that are narrowly tailored and targeted only at qualified investors pose a relatively low risk that they would be received by unqualified investors. On the other hand, however, as we noted in our Concept Release Letter, fund issuers and their fund sponsors expend enormous resources, time, and costs to assess and track that no “general solicitation” or “general advertising” has occurred. Clarifying that these types of targeted communications to qualified investors would not be considered “general solicitation” or “general

¹⁶ Proposal at 17974. “Angel investor group” would be defined as “a group of accredited investors that holds regular meetings and has written processes and procedures for making investment decisions, either individually or among the membership of the group as a whole, and is neither associated nor affiliated with brokers, dealers, or investment advisers.” See proposed Rule 148 and Instruction to Rule 148. Conditions in the proposed rule include that: (a) no advertising for the seminar or meeting references a specific offering of securities by the issuer; (b) the sponsor of the seminar does not (1) make investment recommendations or provide investment advice to attendees of the event, (2) engage in any investment negotiations between the issuer and investors attending the event, (3) charge attendees of the event any fees, other than reasonable administrative fees, (4) receive any compensation for making introductions between event attendees and issuers or for investment negotiations between the parties, and (5) receive compensation with respect to the event that would require it to register as a broker or an adviser; and (c) the information communicated is limited to a notification that the issuer is in the process of offering or planning to offer securities, the type and amount of securities being offered, and the intended use of proceeds of the offering.

advertising” would strike an appropriate balance between allowing these important communications and investor protection.

We thus recommend that the Commission make clear that an issuer that adopts and follows policies and procedures reasonably designed to ensure that communications that are (i) tailored and targeted only towards qualified investors and (ii) not intended to result in a sale to unqualified investors, will not be viewed as having engaged in general solicitation or general advertising with respect to those communications. In addition, because inadvertent foot faults can happen even when an issuer follows reasonably designed policies and procedures, we recommend that the Commission also clarify that such an issuer will not become ineligible to rely on a Regulation D exemption where minimal access to the general public occurs inadvertently.¹⁷

The Commission seeks comment on whether it should permit organizations other than those listed in proposed Rule 148 to act as sponsors of “demo days.”¹⁸ While we believe our above recommendation is a better approach, we ask that, *at a minimum*, the SEC broaden the proposed Rule 148 exemption to permit SEC-registered investment advisers that are sponsors of private funds to be included as an entity that may sponsor a covered “demo day” or similar event. The Commission does not provide any rationale for excluding these investment advisers from being able to rely on proposed Rule 148. Permitting them to rely on the exemption would, in our view, appropriately expand the universe of who could organize events with limited participation by small groups of targeted sophisticated potential investors without undermining the Commission’s investor protection efforts.

C. The Commission Should Adopt Rule 241 as Proposed and Not Limit the Provision of Testing-the-Waters Materials to IAIs and QIBs

The Commission proposes new Rule 241 to permit an issuer to use generic solicitation of interest materials to “test-the-waters,” *i.e.*, gauge investor interest, for an exempt offering of securities before making a determination as to the exemption it will rely on for the offering. The Commission notes that both issuers and investors would benefit from the flexibility the proposed rule would provide. It states in the release that issuers would be able to determine interest before deciding whether to proceed with the offering and which exemption to use, and investors would “potentially have input into the structuring of the offering” and also “be able to convey to the issuer the types of information about which they are most interested, leading ultimately to a

¹⁷ Proposal at 17976 (Question 20). We recommend that the Commission consider formalizing the no-action relief related to offerings by private funds provided in the Division of Corporation Finance’s no-action letter to Lamp Technologies, Inc. (May 29, 1997).

¹⁸ Proposal at 17975 (Question 19).

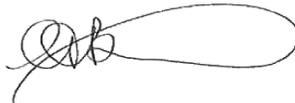
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lower cost of capital for the issuer.”¹⁹ We agree with the Commission’s reasoning and support the proposed exemption.

As proposed, the exemption would be available for communications directed to all types of investors. The Commission asks whether it should limit the provision of testing-the-waters materials to IAIIs and QIBs.²⁰ Given that the purpose of the proposed exemption is to allow issuers to gauge investor interest in a potential exempt offering and that there is often interest by high net worth and ultra-high net worth investors in many types of exempt offerings, we agree with the Commission that limiting this exemption to institutional investors would “significantly undermine its utility.”²¹ Accordingly, we believe that the Commission should not limit the exemption in this way.

We appreciate the Commission’s consideration of our comments on this important Proposal and would be happy to provide any additional information that may be helpful. Please contact the undersigned or Monique Botkin at (202) 293-4222 if we can be of further assistance.

Respectfully Submitted,



Gail C. Bernstein
General Counsel

cc: The Honorable Jay Clayton, Chairman
The Honorable Hester M. Peirce, Commissioner
The Honorable Elad L. Roisman, Commissioner
The Honorable Allison Herren Lee, Commissioner

William Hinman, Director, Division of Corporation Finance
Dalia Blass, Director, Division of Investment Management

¹⁹ Proposal at 17976.

²⁰ Proposal at 17979 (Question 24).

²¹ Proposal at 17977.