

## SEC Expands the Accredited Investor Definition

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### What You Need To Know:

- The SEC is amending the “accredited investor” definition to expand the pool of potential investors in private offerings of securities.
- Family offices, limited liability companies, and other entities with more than \$5 million in assets will now qualify as accredited investors.
- Knowledgeable employees and holders of Series 7, 65, and 82 licenses will be added to the definition of accredited investor.
- The amendments are effective 60 days following formal publication in the Federal Register, likely applicable to closings in November 2020 and thereafter.

On August 26, 2020, the Securities and Exchange Commission (SEC) adopted amendments (the Amendment) to the “accredited investor” definition to broaden the category of potential investors in private offerings of securities exempt from registration pursuant to Regulation D under the Securities Act of 1933, as amended (the Securities Act). While the Amendment can apply to or benefit all issuers of unregistered securities in reliance on Regulation D, this Client Alert focuses on the impact on private funds, as Regulation D is the most commonly used exemption by such funds. Under the current definition, natural persons must have an individual net worth exceeding \$1,000,000 (excluding the value of their primary residence), or an individual income exceeding \$200,000, or a joint income with a spouse exceeding \$300,000. Accredited investor entities are restricted to an enumerated list of entities.

#### Entities

The Amendment expands the list of entities that would qualify as accredited investors, including:

- Family offices with \$5 million in assets not specifically formed for the specific purpose of acquiring the securities offered and whose investment is directed by a person with financial and business knowledge and experience
- Family clients of such qualified family offices
- Limited liability companies with more than \$5 million in assets not specifically formed for the specific purpose of acquiring the securities offered
- SEC- and state-registered investment advisers as well as venture capital or mid-sized private fund exempt reporting advisers under the Investment Advisers Act of 1940
- Entities not covered by the current rule owning more than \$5 million in “investments” (as defined under the Investment Company Act of 1940) not specifically formed for the specific purpose of acquiring the securities offered
  - This change is beneficial to private funds and other issuers that have potential investors that are large,

sophisticated institutions that historically did not meet the technical requirements to qualify as accredited investors.

## Natural Persons

According to the SEC, the accredited investor definition protects persons whose financial sophistication allows them to sustain the risk of losing their investments and who do not need the Securities Act's protections. Previously, wealth was the sole indicator of financial sophistication. The Amendment creates an alternative route for persons without the necessary income to invest in private funds based on the belief that those with sufficient licensing and knowledge can adequately assess risks, including:

- Knowledgeable employees of the private fund offering securities (i.e., high-level executives, heads of principal business units, or qualifying investment personnel)
- Holders of Series 7, 65, or 82 licenses

Additionally, the term "spousal equivalent" is being added to the accredited investor definition, so that spousal equivalents may pool their finances for the purpose of qualifying as accredited investors.

## Qualified Institutional Buyer Definition

The SEC also adopted amendments to the "qualified institutional buyer" definition in Rule 144A under the Securities Act to expand the list of entities that are eligible to qualify as qualified institutional buyers, including:

- Limited liability companies
- Rural business investment companies (RBICs)
- Entities not covered under the current accredited investor rule (such as sovereign funds and non-U.S. plans)

While the Amendment seeks to modernize access to private offerings, actual impact on the total amounts raised and the number of new investors is likely minimal for larger hedge and private equity funds with higher-net-worth individual and institutional investors. Even for these larger private funds with a more institutional investor base, the additional natural person categories may be useful with respect to advisory personnel that want to invest in

private funds sponsored by their employer. Smaller venture capital funds and smaller private placements by operating companies may find these changes more useful in growing their investor base.

## Next Steps

At minimum, the Amendment will require updates to subscription documents and offering materials where accredited investor certification is required.

Please contact one of the listed authors of this Client Alert or another Lowenstein Sandler contact if you have any questions with respect to the Amendment or the applicability of the Amendment to a securities offering, or if you would like assistance reviewing and updating your documents.

For additional information regarding the amendments, please see the following links:

- [SEC Press Release](#)
- [SEC Proposed Amendment](#)

# Contacts

Please contact the listed attorneys for further information on the matters discussed herein.

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