Securities Regulation Daily Wrap Up, CORPORATE FINANCE—Commission addresses policy recommendations from Small Business Forum, (Jul. 29, 2022)

Securities Regulation Daily Wrap Up

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In a new report on the forum, which was held in April, the SEC addresses participants' recommendations for changes to the capital raising framework.

The SEC released a report on the 2022 Small Business Forum in which it provides its responses to policy recommendations made by participants on issues such as access to capital, Regulation Crowdfunding, the "accredited investor" definition, and 3(c)(1) funds. The forum is held annually and gives the public a chance to provide feedback on issues impacting small business and their investors and to provide recommendations to improve capital-raising policy.

In the report the Commission outlines the key policy recommendations from the four-day meeting and provides an answer to each suggestion. The SEC indicated that it will consider Forum recommendations alongside other public comments on the particular policy initiatives.

Equitable access. From the portion of the Forum about empowering entrepreneurs, the participants recommended that the Commission ensure that the capital-raising rules provide equitable access to capital for underrepresented founders and investors. In response, the Commission noted that the Spring 2022 Regulatory Agenda includes initiatives to consider further updates to the rules related to exempt offerings. In connection with any initiative, the agency said that it will consider this recommendation, as well as those received in recent years from the SEC Investor Advisory Committee.

Participants also suggested that in considering changes to the private capital markets, the SEC should ensure that companies have viable pathways to access capital to allow growth and innovation. Again the Commission pointed out that the Spring 2022 Regulatory Agenda includes relevant initiatives. Those include the consideration of rules related to exempt offerings, including potential updates to Regulation D, Form D, and Rule 144.

The Forum participants recommended that the Commission revise Regulation Crowdfunding to permit investment companies to conduct a crowdfunding offering. The agency noted that 1933 Act Section 4A(f)(3) prohibits investment companies from using the Regulation Crowdfunding exemption. The Commission said that because the prohibition on investment companies originates in the statutory provision, an amendment to the Regulation Crowdfunding eligibility criteria would require Congressional action.

Accredited investor definition. The report includes a number of recommendations related to the definition of "accredited investor." First, the Forum attendees suggested that the SEC expand the definition to achieve greater diversity among startup investors and entrepreneurs. The Commission replied that it is considering a potential release seeking public comment on ways to further update the rules related to exempt offerings to more effectively promote investor protection, including updating the financial thresholds in the accredited investor definition.

Next, Forum participants requested that the SEC expand the accredited investor definition to include additional measures of sophistication. The Commission noted that in 2020 it adopted amendments to the definition of "accredited investor" under Regulation D that added new categories of qualifying natural persons and entities. At that time the agency made other modifications to the definition including allowing natural persons to qualify as accredited investors based on certain professional certifications, designations, or credentials. The Commission may consider designating additional qualifying professional certifications, designations, and other credentials by order, and will take into account the Forum recommendation if it pursues an initiative related to exempt offerings.

The Forum attendees also asked the SEC to expand the accredited investor definition to include any person who invests not more than 10% of the greater of his/her annual income or net assets. Another recommendation pertained to raising the wealth thresholds in the accredited investor definition, and asked the SEC to consider the unintended consequences on access to capital in under-resourced and underrepresented communities. To both recommendations, the SEC pointed to the potential upcoming release on ways to update the rules related to exempt offerings to more effectively promote investor protection, including possible updates to the financial thresholds in the definition.

Fund managers. From the portion of the Forum that focused on fund managers, the participants recommended that the Commission create a new private fund exemption to allow states to foster intrastate and regional funds focused on community-based investing that is open to non-accredited investors. The SEC said that in connection with increasing access to capital, the Commission adopted a set of rule amendments designed to facilitate capital formation and increase opportunities for investors by expanding access to capital for small and medium-sized businesses and entrepreneurs. In addition, in 2021 and 2022 the SEC's Small Business Capital Formation Advisory Committee has met and discussed how the accredited investor definition impacts capital raising opportunities for early-stage companies that raise capital through exempt offerings.

Another recommendation was to increase the thresholds allowed in 3(c)(1) funds to achieve greater diversity among startup investors and entrepreneurs. The Commission noted that a qualifying venture capital fund is a type of private fund that is excluded from the definition of "investment company" under Investment Company Act Section 3(c)(1), so any amendments to Section 3(c)(1) would require Congressional action. The Commission provided the same feedback on a recommendation to increase the number of investors allowed in 3(c)(1) funds above 99 investors.

One of the other Forum suggestions related to ESG regulations under consideration by the Commission. Specifically, participants recommended that the agency consider the impact of the proposed ESG regulations on small and medium-sized companies, including whether such requirements will discourage companies from going public.

The Commission stated that in the ESG proposing release the SEC solicits comment on whether the Commission should consider scaled disclosure requirements for smaller reporting companies and certain other categories of registrants. In addition, the proposed amendments include certain disclosure accommodations, including an exemption from the Scope 3 emissions disclosure requirement for smaller reporting companies and a longer transition period to comply with the proposed rules for smaller reporting companies. The Commission indicated that it will consider this Forum recommendation in connection with the proposed ESG rules.

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