# Securities Regulation Daily Wrap Up, SEC NEWS–Bigger pool of investors should be allowed to invest in private offerings, Uyeda says, (Jan 23, 2024)

By Suzanne Cosgrove

The SEC commissioner noted amendments to Regulation D, including an accredited investor definition, are on this year's Commission rulemaking schedule.

The current regulatory regime for raising capital without registration needs streamlining, SEC Commissioner Mark Uyeda told an industry group this week. "Normally, having choices is a good thing," he added in remarks at the 51st Annual Securities Regulation Institute. "However, even the most sophisticated securities lawyers often need a chart to track the different exemptions across the various factors."

In addition to private offerings under section 4(a)(2) and its safe harbor, rule 506(b), there are at least five other categories of exemptions, Uyeda noted: (1) rule 506(c) under the Securities Act; (2) rule 504 under the Securities Act; (3) Regulation A, including tier 1 and tier 2; (4) Regulation Crowdfunding; and (5) the intrastate exemptions under section 3(a)(11) of the Securities Act and rules 147 and 147A.

"Each exemption differs on particular factors, such as whether general solicitation is permitted, the types of issuers that can use the exemption, the types of investors that can purchase under the exemption, the amount of disclosure required, whether securities sold pursuant to the exemption are 'restricted,' and whether the exemption preempts state blue sky requirements," Uyeda told the group.

"Our regulatory regime should have an offering exemption tailored to each of the common capital raising scenarios," he said. For example, "the requirements to raise capital for a start-up company in the 'friends and family' round should be different from the requirements to raise capital for a billion-dollar company shortly before its IPO."

**Expanding retail opportunities.** Beyond discussions of how to qualify as an accredited investor, or what disclosure should be required in rule 506(b) offerings, the Commission also should consider the long-term, real-world impacts that any rulemaking will have on retail investors and entrepreneurs, particularly those from historically underrepresented backgrounds, Uyeda said.

Regulation D includes two SEC rules -- *Rules 504* and *506* -- that issuers often rely on to sell securities in unregistered offerings. Most private placements are conducted in accordance with Rule 506.

Currently, a company relying on rule 506(b) can sell to up to 35 non-accredited investors, he noted. However, if there are any non-accredited investors, the company must provide disclosure information equivalent to what is required in a Regulation A offering. Because of this requirement, companies relying on rule 506(b) often do not permit participation by non-accredited investors, he said.

The implication of the current rule -- and current market practice -- is that many non-accredited investors are not given an opportunity to invest in private companies, Uyeda added, even when they are able to assess the investments' risks and rewards.

**Controversial metrics.** Since its inception in 1982, the definition of an accredited investor has required an individual have net worth in excess of $1 million or $200,000 in annual income. Some have since advocated for inflation-based amendments to that definition. However, simply adjusting the thresholds for inflation assumes that the amounts established in 1982 are the correct metrics for eligibility to participate in private offerings, Uyeda said.

In the year after the net worth and annual income thresholds were initially adopted, approximately 1.8 percent of U.S. households qualified as an accredited investor, he said. If net worth and annual income levels could be adjusted for

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inflation from 1982 to 2022 dollars, approximately 6.5 percent of U.S. households would have qualified as accredited investors.

“It is unclear why having fewer accredited investors, whether at 6.5 percent or 1.8 percent of U.S. households, is preferrable to having more accredited investors,” Uyeda said. Increasing net worth and annual income requirements also would have a disproportionate impact on racially and ethnically diverse investors and younger investors, he said. In addition, a reduction in the pool of diverse accredited investors may adversely affect the ability of persons of color to finance their start-ups.

**A sliding-scale approach.** Instead of adjusting net worth and annual income thresholds for inflation, “we should consider new approaches to defining the pool of investors that can invest in private companies,” he suggested. “One possibility is to create a sliding scale approach and allow any individual to invest at least a small amount in private companies over the course of a year.”

With a sliding scale approach, a person would be able to invest up to a certain percentage, based on a personal financial metric, in private companies during a rolling time period, Uyeda said. The percentage would increase along with the value of the financial metric. For example, if a person’s securities investments were less than $100,000, then the person could invest up to 5 percent of the amount in private companies during a rolling 12-month period.

“These investors and entrepreneurs are concerned about opportunity,” he said. “For investors, it is the opportunity to build wealth through investments, even if it is a limited amount of money each year. For entrepreneurs, it is the opportunity to access an adequate pool of capital to fund a business idea.”

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