

Securities and Exchange Commission Final Rules to Amend the Definition of “Accredited Investor” (Adopted by the SEC on August 26th, 2020).

The SEC [voted 3-2](#) to amend the current definition of an “accredited investor” under Rule 501 of Regulation D. The rule expands the criteria required for an investor to be deemed accredited beyond the current income and net worth thresholds to include individuals that hold certain licenses or certifications that demonstrate financial sophistication. The SEC’s efforts were informed by a [2015 staff report](#) on the accredited investor definition, comments received from a [June 2019 concept release](#) on private offerings, as well as [initiatives by Congress](#) to expand the definition. The SEC initially proposed this rule in December 2019; the final rules closely track the proposal.

Background

The unregistered offering market has grown significantly in recent years, with \$1.56 trillion being raised in Rule 506 offerings during 2019 (compared to \$1.2 trillion in registered offerings). In order to invest in such offerings, an investor typically needs to be either an institutional buyer or be an accredited investor under Rule 501. The current accredited investor definition provides that an individual is accredited if they meet any of the following criteria:

- They have a net worth exceeding \$1 million (excluding their primary residence) either alone or with their spouse;
- They have earned at least \$200,000 of income in the previous two years (or \$300,000 jointly with a spouse) and have a reasonable expectation of earning that same income in the coming year; or
- They are a director, executive officer, or general partner of the issuer

Changes to Accredited Investor Definition

The final rule would maintain the existing wealth test thresholds and provide and incrementally provide an alternative path for individuals or entities to be deemed accredited. The expansion is based upon certain licenses or professional certifications held by individuals:

- The SEC’s initial order includes individuals that hold (in good standing) FINRA Series 7, 65, or 82 licenses
- The SEC may expand this list in the future, by order, to include other FINRA or SEC licenses, or certifications such as a CPA or CFA. The list could also potentially encompass certain educational credentials such as an MBA.
- The final rule represents an incremental approach by the SEC to expand the list of eligible individuals “after first gaining experience with the revised rules.”

“Knowledgeable employees” of private funds

- The final rule includes knowledgeable employees of private funds – as defined in Rule 3c-5(a)(4) - in the definition of accredited investor. This would include trustees and advisory board members of Section 3(c)(1) or 3(c)(7) funds, as well as employees of the fund who “have participated in the investment activities of such private fund for at least 12 months.”

RBICs / LLCs / Family Offices / Spousal Equivalents

- The final rule also includes rural business investment companies (RBICs) in the definition, bringing their treatment in line with SBICs
- LLCs with at least \$5 million in assets and which were not formed “for the specific purpose of acquiring the securities being offered” are also included, as are family offices with at least \$5 million in assets
- The Commission also clarified that spousal income or net worth can be used when calculating financial thresholds for eligibility, and that securities need not be purchased jointly if such equivalents are used
- There is also a “catch-all” category for entities, including Indian tribes, that own investments in excess of \$5 million, provided that such entities were not formed for the purpose of investing in the securities offered

Qualified Institutional Buyer (QIB) Definition

- The final rule expands the definition of a QIB to include LLCs and RBICs if they have \$100 million in securities owned and invested provided that they satisfy the test for QIB status