Recommendation of the Investor as Purchaser Subcommittee and the Investor Education Subcommittee: Accredited Investor Definition

Preliminary Observations:

- The Securities Act of 1933 provides an exemption from registration and disclosure requirements for transactions “not involving any public offering.” However, in drafting the legislation, Congress did not clearly spell out what distinguishes a “public” from a “private” offering.

- In 1953, the Supreme Court ruled that availability of the exemption “should turn on whether the particular class of persons affected needs the protection of the Act.”[1] Specifically, the court stated, “An offering to those who are shown to be able to fend for themselves is a transaction ‘not involving any public offering.’”

- Private offerings inherently have limited secondary market liquidity, and the pricing of such securities is less transparent since they are not traded in the public securities market. In addition, the initial and on-going disclosure obligations of the issuers of such securities are not subject to the same Commission rules, but rather are determined exclusively by the issuer or are subject to negotiation and agreement between the issuer and the investor. These attributes make private investments more appropriate for sophisticated investors who understand these risks and have the ability to negotiate access to information.

- The Commission has adopted a number of regulations over the years seeking to clarify when and how issuers can conduct offerings of securities without triggering the ’33 Act’s registration and disclosure requirements. Today, the private securities markets rival the public markets in size, and the vast majority of private offerings are conducted in reliance on Rule 506 of Regulation D.

- Rule 506 allows for sales to an unlimited number of “accredited investors” and, for offerings that do not involve general solicitation, to a limited number of sophisticated non-accredited investors. (These non-accredited investors must either possess sufficient financial knowledge on their own or be advised by a purchaser representative who has the necessary sophistication.)

- As a result, the accredited investor definition has come to play a central role in determining whether an offering qualifies for the private offering exemption. Questions have been raised, however, over whether the current definition effectively defines a class of individuals who are able to “fend for themselves” without the protections afforded by the ’33 Act.

[1] Securities and Exchange Commission v. Ralston-Purina Co., 346 U.S. 119, 73 S.Ct. 981, 97 L.Ed. 1494 (1953).

- Reflecting those concerns, this Committee earlier recommended that the Commission revise the accredited definition, as it pertains to natural persons, to reflect the loss of procedural protections once afforded by the general solicitation and advertising ban. Moreover, while the public debate over the accredited investor definition has primarily focused on whether the financial thresholds should be increased, the Committee has encouraged the Commission to consider alternative formulations in attempting to arrive at an appropriate definition.

Recommendation

As the Commission conducts its review of the accredited investor definition, as mandated by the Dodd-Frank Wall Street Reform and Consumer Protection Act, it should seek to determine whether the current definition achieves the goal of identifying a class of individuals who do not need the '33 Act protections in order to be able to make an informed investment decision and protect their own interests. The Committee does not believe that the current definition as it pertains to natural persons effectively serves this function in all instances. We therefore encourage the Commission to consider alternative approaches that would better protect vulnerable investors without unnecessarily constraining the supply of capital in the private offering market, including approaches that would enable individuals to qualify as accredited investors based on their financial sophistication, consideration of whether financial thresholds need to be adjusted for inflation, as well as alternative approaches to setting financial thresholds. Finally, the Committee believes that protections for non-accredited investors who rely on recommendations from purchaser representatives to qualify as sophisticated should be strengthened.

Recommendation 1

The Commission should carefully evaluate whether the accredited investor definition, as it pertains to natural persons, is effective in identifying a class of individuals who do not need the protections afforded by the '33 Act. If, as the Committee expects, a closer analysis reveals that a significant percentage of individuals who currently qualify as accredited investors are not in fact capable of protecting their own interests, the Commission should promptly initiate rulemaking to revise the definition to better achieve its intended goal.

Supporting Rationale

Over the years, analysis of whether a particular class of individuals needs the protections of the Act has generally turned on three factors: 1) whether the individuals have (or are able to negotiate) access "to the same kind of information that the Act would make available in the form of a registration statement;"[2] 2) whether the individuals can bear the economic risks of the offering, including risks associated with the illiquidity of private offerings and the risk of loss; and 3) whether the individuals are sufficiently financially sophisticated, based on their knowledge and experience and in particular their ability to evaluate risks and merits, to make an

[2] Ibid.

informed investment decision without the full disclosure provided in a public offering. [3] These seem to us to be generally appropriate criteria to use in making this determination.

The current definition's financial thresholds serve as an imperfect proxy for sophistication, access to information, and ability to withstand losses.

The current accredited investor definition for natural persons uses financial thresholds based on income and net worth as proxies for access to information, financial sophistication, and ability to withstand potential losses. It is true that some individuals who meet the income and net worth criteria of the definition will also be financially sophisticated, and some may be able to gain access to information of the type provided in public company registration statements. However, there is nothing in the definition itself that guarantees that this will be the case. Indeed, the limited data that exists suggests that though there is a correlation between income and financial literacy, a significant percentage of even the wealthiest investors score poorly on tests of basic financial literacy. Such tests don't begin to measure the type or level of financial sophistication needed to evaluate the potential risks and benefits of private offerings.[4] At the same time, individuals who fail to meet the financial thresholds in the current definition may possess the financial sophistication and access to information necessary to make an informed investment decision. In other words, the current definition is, at best, a highly imperfect proxy for financial sophistication and access to information.

There is a more apparent connection between the financial thresholds in the current definition and the ability to withstand the potential losses if their investment fails. Even here, however, there are several reasons why we question whether the current income and net worth thresholds reliably provide that assurance.

- First, while the value of the primary residence has been excluded from the net worth calculation used to determine accredited investor status, other non-financial assets have not. As a result, the current definition of net worth does not guarantee that the individual accredited investor will in fact have sufficient liquid financial assets to ensure either that they can hold the securities indefinitely or that they can withstand a significant loss on those investments. For example, a person whose net worth is based largely on ownership of a family farm or other closely-held business could be forced to sell that farm or business if they are heavily invested in an illiquid private offering and find themselves in need of cash.

- Second, many individuals who meet the net worth threshold will do so based on a retirement nest egg that they rely on to provide regular income that will need to last them throughout their remaining years. For example, while only about 6.7 percent of households overall have a net worth excluding the value of the primary residence of $1

[3] These latter two factors are reflected in Rule 146, which was adopted in 1974 as a predecessor to Rule 506.
[4] For example, high income individuals got an average score of 3.42 on the FINRA Investor Education Foundation's 2009 National Survey of Financial Capability in the United States, which uses a 5-point scale, compared with an overall average of 2.72. However, the survey tests knowledge of such basic concepts as the effect of inflation, compound interest, diversification, mortgages, and the correlation between interest rates and bond prices; it does not measure financial sophistication at a level relevant to this issue.

million or more, according to an analysis based on figures from the 2010 Survey of Consumer Finances, roughly 9.7 percent of households headed by someone 65 or older meet that threshold, as do approximately 12 percent of households headed by someone between the ages of 50 and 64.[5] While some of those retirees and near retirees will be easily able to absorb the potential losses associated with private offerings, others who comfortably meet the threshold would nonetheless see their retirement security put at risk as a result of such losses. The illiquidity of private offerings also poses a particular challenge for those who are relying on their investments as a source of regular income to meet monthly living expenses.

- Third, while many individuals who meet the income threshold will also have significant financial assets, the income test standing by itself does not provide any such assurance. The ability to withstand potential risks of private offerings among individuals who qualify as accredited investors based exclusively on income will vary greatly based on a number of factors, including whether they also have substantial assets, albeit less than the $1 million in net worth required to qualify as accredited, how heavily invested they are in private offerings, and how many working years they have left to recover financially if they suffer a substantial loss.[6]

In short, while reliance on income and net worth thresholds results in a definition that is clear and relatively simple to implement, this approach over-simplifies the factors that determine whether an individual truly has the wealth and liquidity to shoulder the potential risks of private offerings. Moreover, the income and net worth thresholds have been seriously eroded by inflation since they were first set in 1982. Had the thresholds been adjusted for inflation, the income threshold today would be just under $500,000 ($740,000 for a married couple) and the net worth threshold would be nearly $2.5 million. While the recent exclusion of the value of the home from the net worth calculation had a considerable impact, particularly in those regions of the country where housing prices are especially high, inflation has nonetheless left the thresholds significantly less restrictive today than they were when they were originally set. A common perception would be that one million dollars represented real wealth in 1982. That isn't necessarily the case in 2014.

Simply adjusting the thresholds for inflation may not be the answer.

For all the reasons listed above, we question whether the current definition meets the standard set by the Supreme Court of identifying a class of individuals who can fend for themselves. We are not, however, simply recommending that the Commission increase the income and net worth thresholds to reflect inflation since 1982. First, we do not know with any certainty whether the Commission found exactly the right level when it set those thresholds originally. It is equally possible that they were set either too low or too high to provide the

[5] *Protecting Investors with the SEC's Accredited Investor Definition*, prepared by staff at AARP using data from the Federal Reserve Board's 2010 Survey of Consumer Finances. Using the same source, the SEC estimates that 7.4 million households qualify as accredited investors based on net worth excluding the value of the primary residence. However, the Commission does not break the number out by age groups.

[6] In every case described above, the degree of risk to the investor would also vary based on the size of the individual's investments in private offerings, as we discuss in greater detail under recommendation 3.

needed investor protections. Moreover, the investing population has changed significantly since that time, with a larger percentage of unsophisticated, middle income individuals turning to the securities markets to save for retirement today than did so 30 years ago. The complexity of financial products, including financial products sold through private offerings, has also grown in the intervening years. Thus, thresholds that made sense for the investing population of 1982 may or may not make sense in 2014.

Second, concerns have been raised that adjusting the thresholds for inflation could significantly restrict the pool of capital available for private offerings. Based on the available information, it is difficult to know precisely what the impact would be. Figures presented in the Commission's general solicitation final rule release suggest that adjusting the net worth threshold for inflation would exclude roughly 60 percent of the households that currently qualify as accredited based on net worth. On the other hand, the Commission has also noted that "only a small percentage of these households are likely to participate in securities offerings, especially exempt offerings." Thus, it is not clear what percentage of accredited investors who actively participate in private offerings would be affected. A survey of its members by the Angel Capital Association suggests that the impact could be much smaller than the raw numbers indicate, but still significant. Based on its survey, ACA concluded that roughly 28 percent of its current members would no longer qualify as accredited if the 1982 thresholds were adjusted for inflation.[7] However, we do not know how representative ACA members are of the broader, active accredited investor population. Nor do we know what percentage of those who would no longer be accredited could still qualify to invest as sophisticated non-accredited investors in Rule 506 offerings that do not include general solicitation.

> <u>The Commission should adopt our earlier recommendations regarding Reg D information collection in order to permit more informed policy decisions with regard to Reg D in general and the accredited investor definition in particular.</u>

One thing that is evident is the degree to which the Commission is currently acting based on incomplete information when it comes to developing policy with regard to Rule 506 offerings, including with regard to the accredited investor definition. As the Commission noted in the release for the final rule lifting the ban on general solicitation in Rule 506 offerings, it has "relatively little information on the types and number of investors in Rule 506 offerings." This makes it difficult if not impossible for the Commission to reliably measure the likely impact of any changes to the accredited investor definition. This should not be seen as an excuse for inaction, however. Rather, the Commission should take immediate steps to collect the data that would allow it to better assess its policy options going forward.

One reason for the dearth of information is that the Commission relies on Form D filings for data, and an unknown but apparently significant percentage of issuers do not file Form D. Moreover, because there isn't a general requirement under Rule 506 for reporting after the initial filing, the information for even those issuers that do comply with the filing requirement may be incomplete. These problems could be remedied, or at least ameliorated, if the Commission were to adopt the reforms to the Rule 506 filing process advocated by this Committee in its first

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[7] Angel Capital Association, *Protect Angel Funding: The Accredited Investor Definition*, ACA Public Policy Update, June 11, 2014 webinar slides.

recommendation, some of which are reflected in the second set of general solicitation rules that the Commission has proposed but not finalized. We urge the Commission to do so. In the meantime, the Commission has indicated that it will be actively monitoring developments in the Reg D market in the wake of the rulemaking lifting the ban on general solicitation. We urge the Commission, as part of that process, to gather information that would help it assess the likely impact of changes in the accredited investor definition on both investor protection and capital formation.

Alternative approaches, as discussed below, could be more effective than the current definition in defining a class of individuals capable of fending for themselves.

A final reason that we are not simply recommending an increase in the income and net worth thresholds is that we question whether simply raising the financial thresholds would best resolve short-comings in the current definition. Alternative approaches, such as basing the definition on financial assets or liquid assets, may be more appropriate than simply raising the existing thresholds. (Canada, for example, bases its definition on either $1 million in financial assets or net assets in excess of $5 million.) Similarly, there may be certain types of financial assets, such as retirement accounts, that should not be included in the calculation. Alternatively, restricting the percentage of assets that individuals could invest in private offerings could lessen the risks for investors without further limiting the pool of accredited investors. Moving away from an approach based strictly on financial capability, a definition that incorporates an experience or sophistication measure may be more effective in identifying a population of individuals who can fend for themselves without unnecessarily constraining the pool of capital available for private offerings.

Each of these approaches offers trade-offs that should be carefully evaluated. We discuss several of them in greater detail below. What is important, as a preliminary matter, is that, as the Commission considers whether to revise the accredited investor definition, it not simply make a binary decision over whether or not to adjust the thresholds to reflect inflation. It should also consider whether the current approach of relying on income and net worth minus the value of the home makes sense or whether an alternative approach would be more effective. Whatever approach the Commission chooses to adopt, it must be able to articulate a reasonable basis for concluding that, under its proposed approach, individuals who meet the definition truly are capable of fending for themselves without the protections afforded in a public offering or, at the very least, of bearing the economic risks of such offerings.

Recommendation 2

The Commission should revise the definition to enable individuals to qualify as accredited investors based on their financial sophistication.

Supporting Rationale

Under the JOBS Act, Rule 506 offerings that include general solicitation can only be sold to accredited investors. As a result, there is currently no means for sophisticated investors who do not meet the financial thresholds in the accredited investor definition to invest in such

offerings. Yet such individuals may be better equipped to assess the appropriateness of investing in private offerings than are individuals who meet the financial thresholds but lack financial sophistication. The Committee believes the Commission should develop a means for sophisticated investors to qualify as accredited. We recognize, however, that, while the logic of doing so seems obvious, finding an acceptable approach is more challenging. Each of the three primary means by which one might measure an individual's financial sophistication for this purpose -- professional credentials, investment experience, a test of relevant financial knowledge -- has limitations. We nonetheless believe this approach offers potential benefits that are worth exploring.

Individuals who have attained certain professional credentials, or who have relevant professional experience, seem like logical candidates to qualify as accredited investors without regard to their income or net worth. The question here is where to draw the line. Two credentials that are commonly mentioned as satisfying this standard are the series 7 securities license and the Chartered Financial Analyst designation. Both are easily defensible as measures of relevant financial sophistication. The risk to the Commission of pursuing this approach is that many other credentials with less claim to measure relevant expertise are likely to seek inclusion on a list of qualifying credentials. In deciding where to draw the line, the Commission should look to whether the credential tests knowledge relevant to the evaluation of securities offerings. The credentialing organization should require an expansive curriculum, thorough examination requirements, and continuing education or training.

If the Commission were to adopt this approach, it would make sense to look beyond credentials and also identify certain individuals whose professional experience qualifies them as financial experts for this purpose. The Commission could, for example, draw on the definition of knowledgeable employee to determine which categories of financial industry employees should be deemed to meet this standard. The United Kingdom recognizes as financially sophisticated for this purpose individuals who are working, or have worked in the prior two years, in a professional capacity in the private equity sector, or in the provision of finance for small and medium enterprises, as well as individuals who are or have been in the prior two years a director of a company with an annual turnover of at least £1 million. It is unclear how many individuals would be added to the pool of eligible investors based on this approach, but it seems like a reasonable approach regardless of the extent of the impact.

A second possible approach is to enable individuals to qualify as accredited investors based on investment experience. The question here again is what form and level of investment experience would qualify. The Commission proposed an "investments owned" test as an alternative basis for determining accredited investor status in its 2007 release, *Revisions of Limited Offering Exemptions in Regulation D*.[8] The United Kingdom allows individuals to self-certify as sophisticated based on one of several factors, including membership in a network or syndicate of business angels and recent prior experience investing in unlisted companies. Participation in an angel network, in and of itself, may not serve as an adequate measure of financial expertise or experience. However, it may be possible to develop an acceptable approach to qualifying as an accredited investor based on participation in an angel group that follows best practices with regard to due diligence and that includes financially sophisticated

[8] Release No, 33-8828: IC-27922: File No. S7-17-07.

members. Given the important role that angel investors play in the funding of Reg D offerings, this seems like an avenue that is worth further exploration.

Finally, it would be possible, at least in theory, to develop a test that individuals could take to qualify as accredited investors. Such a test could be developed either by the regulators themselves -- the SEC working in conjunction with the state securities regulators and FINRA -- or it could be developed by an independent party. If the latter, regulators would need to be satisfied that the test was rigorous enough to indicate a reasonable level of relevant financial expertise. It is unclear, however, how many individuals would be willing and able to qualify as accredited investors through this means.

Non-accredited investors are able to qualify as sophisticated based on their reliance on a recommendation from a purchaser representative. As discussed below, the Committee believes investor protections associated with reliance on a recommendation from a purchaser representative need to be strengthened. If and only if those improved protections were adopted and proved successful, the Commission could consider permitting individuals to qualify as accredited through a similar means of relying on the recommendation of a fiduciary adviser with no direct or indirect financial stake in the offering.

Recommendation 3

If the Commission chooses to continue with an approach that relies exclusively or mainly on financial thresholds, the Commission should consider alternative approaches to setting such thresholds – in particular limiting investments in private offerings to a percentage of assets or income – which could better protect investors without unnecessarily shrinking the pool of accredited investors.

Supporting Rationale

The chief benefit of a definition based on income or net worth is that it is relatively simple and straightforward to implement. As the above discussion is intended to illustrate, however, that simplicity can also be a problem, given the complex factors that affect whether an individual is in fact financially capable of shouldering the risks associated with private offerings. Changes to this approach, such as basing thresholds on financial assets or excluding retirement accounts, could address certain of those factors most relevant to investor risk. But care would have to be taken to ensure that the revised thresholds were not easily circumvented, by encouraging individuals to withdraw money from retirement accounts in order to qualify, for example. Moreover, such changes could add to the complexity of the definition and thus make it more difficult to implement. Thus, while we believe these approaches have benefits over the current approach that are worth exploring, we also believe an alternative approach based on percentage of assets or income has the potential to offer a better solution.

The risks associated with investing in private offerings are greatly affected by how heavily the individual invests in such offerings. For example, an individual with $200,000 in income who invests $5,000 in a private offering is unlikely to suffer irreversible financial harm. The same cannot necessarily be said if that individual invests $50,000 or $100,000. That

difference in risk is not reflected in the current definition. Instead, under the current definition, an individual with a net worth of $999,000 can't invest a dime in Rule 506 offerings, but an individual with a net worth of $1 million can risk it all. Similarly, an income of $200,000 per individual (or $300,000 per couple) allows unlimited investment in Rule 506 offerings, while individuals making just slightly less are shut out entirely.

Leaving aside the question of whether the financial thresholds are currently set at an appropriate level, the basic "on/off switch" approach seems illogical. A more sensible approach might be to allow some investments in private securities once a person reaches an initial threshold, based on percentage of income or assets, with restrictions being reduced and then eliminated as income or assets rise. Such an approach would significantly reduce the risk that unsophisticated investors would suffer unaffordable losses, which should in our view be the central aim of a definition based on financial capability.

For example, *and for purposes of illustration only*, the Commission could retain the current income and net worth thresholds as the base value for the accredited investor definition, but restrict individuals who meet these thresholds to investing up to 10 percent of their income or net worth in private offerings in aggregate in a 12-month period. At the same time, the Commission could use the thresholds as adjusted for inflation to define the level above which private offering investments would not be subject to any such limits.[9] We offer this example for illustrative purposes only and not to suggest that these are the thresholds the Commission should adopt. On the contrary, if the Commission chose to adopt this approach, it would need to have a reasonable basis for determining: 1) the level of income or net worth at which any investment in Rule 506 offerings would be permissible for individuals who do not meet the sophistication standard required for non-accredited investors; and 2) above what level (if any) it would be appropriate not to impose any limitations on investment in Rule 506 offerings for individuals. It would also need to determine the percentages of income or net worth that would be appropriate at different income and net worth levels and whether it would be appropriate to incorporate a sophistication or experience requirement in the definition where no limitations are placed on investments in private offerings.

Properly structured, such an approach to setting the accredited investor definition could significantly reduce the likelihood that investors would suffer unaffordable losses without shrinking the pool of accredited investors in the way that simply adjusting the thresholds for inflation would be likely to do. Moreover, it could work as a stand-alone approach to setting the definition or in combination with a sophistication or experience criteria, as discussed above.

Recommendation 4

The Commission should take concrete steps encourage development of an alternative means of verifying accredited investor status that shifts the burden away from issuers who may, in some cases, be poorly equipped to conduct that verification, particularly if the accredited investor definition is made more complex.

Supporting Rationale

[9] The Committee is not suggesting any changes to the qualified purchaser definition.

The Committee has previously noted the benefits of relying on reliable third parties to perform verification of accredited investor status. Such an approach better protects investors from having to share potentially sensitive financial information with issuers in order to participate in offerings. It also reduces the compliance burden for the small issuers who turn to the Reg D market to raise capital. We believe those benefits become even more compelling when contemplating improvements to the accredited investor definition.

One of the concerns most frequently raised by the issuer community is the challenge of verifying accredited investor status, a challenge that only increases if the definition is made more complex. This implementation concern has caused some who recognize shortcomings in the existing accredited investor definition to nonetheless resist changes that would make the definition more complex. For example, setting financial thresholds based on a percentage of assets or income, as discussed above, has the potential to greatly reduce potential risks to investors without reducing the pool of capital available for private offerings. Yet, without an alternative means of verifying accredited investor status, this approach would either have to rely on self-certification, which many investor advocates have found unacceptable, or would impose significant verification burdens that issuers would find difficult if not impossible to undertake. Similar concerns are likely to be raised with regard to recommendations to base financial thresholds on financial assets, or to back retirement accounts out of the net worth calculation.

Those concerns could be reduced, if not eliminated, if an independent third party existed to perform this function. For such a system to work, the third party verifier would need to be subject to appropriate standards, with regard to accuracy, privacy and information security, for example. Some degree of regulatory oversight or at least accountability would be needed to ensure adherence to these standards. Securities professionals, such as brokers and investment advisers, accountants, and attorneys[10] would all appear to be well situated to provide such services. Alternatively, an entity could emerge with a business based specifically on providing these verification services.

Both because of the broader benefits of encouraging third-party verification, and because of its implications for improving the accredited investor definition, the Committee strongly encourages the Commission to develop an approach to third-party verification that actively encourages the availability of such services. The Commission should begin by studying the current state of the market with regard to verification practices. Its analysis should look specifically at: whether third-party verification services are readily available at a price that makes them affordable for small issuers; who is currently offering such services and under what circumstances; whether impediments currently exist that restrict the availability of such services; and what additional steps, if any, are needed to encourage further development of such services.

Recommendation 5

In addition to any changes to the accredited investor standard, the Commission should strengthen the protections that apply when non-accredited individuals, who do not otherwise

[10] While bar association membership does not provide the same type of regulatory oversight that exists for brokers and investment advisers, through the SEC and state securities regulators, or accountants, through the PCAOB, it does provide for a level of professional accountability.

meet the sophistication test for such investors, qualify to invest solely by virtue of relying on advice from a purchaser representative. Specifically, the Committee recommends that in such circumstances the Commission prohibit individuals who are acting as purchaser representatives in a professional capacity from having any personal financial stake in the investment being recommended, prohibit such purchaser representatives from accepting direct or indirect compensation or payment from the issuer, and require purchaser representatives who are compensated by the purchaser to accept a fiduciary duty to act in the best interests of the purchaser.

Supporting Rationale

In offerings that do not involve general solicitation, Rule 506 allows for purchases by up to 35 non-accredited investors who, alone or with a purchaser representative, must be sophisticated. Relying on a purchaser representative enables individuals who might not otherwise qualify as accredited investors or as sophisticated non-accredited investors to invest in Rule 506 offerings. Properly structured, such an approach can serve the interests of investors and issuers alike.

Unfortunately, the Commission's rules do not, in our view, achieve an appropriate balance. They allow unsophisticated, non-accredited investors to invest in private offerings in reliance on a recommendation from a purchaser representative who may have significant conflicts of interest and who isn't subject to a clear legal obligation to act in the best interests of the investor. While the regulations place some restrictions on purchaser representatives, they still allow them to be paid by the issuer and to have a considerable financial stake in the success of the offering, so long as that financial interest is disclosed to the investor. Such disclosures are notoriously ineffective in protecting investors from harm, as was well documented in the SEC's 2012 financial literacy study.

Where a purchaser representative is serving in a professional capacity (and not simply providing uncompensated advice to a friend or family member, for example), we believe the appropriate approach is to eliminate financial conflicts of interest to the degree possible. Moreover, the degree of reliance that exists in such a relationship is consistent with a fiduciary duty, which we believe should be spelled out as part of the rules governing purchaser representatives who perform this function in a professional capacity. Even with these changes, activities of those professional purchaser representatives who are not separately regulated as broker-dealers or investment advisers could be extremely difficult for regulators to monitor. The Commission should consider whether some form of notice to regulators should be required of any and all individuals or entities who wish to serve as paid purchaser representatives or whether additional oversight of such individuals is necessary and appropriate.[11]

[11] To be clear, the Committee is not recommending that individuals who serve informally as uncompensated purchaser representatives for friends or family members be regulated.