DEMOCRATIZING OPPORTUNITIES TO "INVEST IN WHAT YOU KNOW": A PROPOSAL TO EXPAND ACCESS TO EXEMPT OFFERINGS FOR INTRA-INDUSTRY EXPERTS

ZEV G. BEEBER*

ABSTRACT

Exempt securities offerings are more popular than registered public offerings, yet the number of investors eligible to participate in the former remains relatively minuscule. The SEC has long utilized wealth tests to determine eligibility for investment in the private markets. Commentators have criticized this phenomenon, in which a limited class of wealthy investors can access attractive exempt offerings, for exacerbating economic, social, and political inequalities in the U.S. For example, SEC Commissioner Elad Roisman described it as "fundamentally unfair, unequal, and unjustified."

Last year, the SEC took a commendable first step toward democratizing access to the private markets by expanding the accredited investor definition. It acknowledged that wealth should not be the sole means of measuring sophistication, a cornerstone of accredited investor status, and identified initial opportunities to promote greater capital formation. The SEC should continue this democratizing effort by recognizing another class of investors who can fend for themselves—intra-industry experts.

Intra-industry experts are not ordinary retail investors. They possess superior, specialized operational or technical knowledge, which they can effectively utilize to evaluate private investment opportunities in their industry. This Article proposes granting accredited investor status to these experts based on their industry-specific sophistication and considers various mechanics for implementing this change. Although similar proposals have appeared in other realms of intellectual discourse, this Article represents the first attempt that the author has found to present this argument in a work of written academic scholarship.

---

* Associate at King & Spalding LLP, McLean, Virginia; J.D., Georgetown University Law Center; B.A., University of Virginia. I am deeply grateful to Professor John F. Olson, Professor David M. Lynn, and Professor James Lopez for their guidance and encouragement in developing this Article. I also extend sincere thanks to Gregory C. Yadley, Esq., a partner in Shumaker, Loop & Kendrick, LLP, Tampa, Florida for his contributions and feedback.

Providing intra-industry experts with access to the private markets would mark a meaningful and responsible advancement toward creating a more equitable landscape of investment opportunities. Though elite in terms of formal education or professional certifications, many of these investors may lack the financial resources to otherwise achieve accredited investor status. Enabling their private market participation would promote economic fairness, facilitate capital formation, and benefit small-business issuers in need of expert advice.

TABLE OF CONTENTS

INTRODUCTION 3
II. EVOLUTION OF THE EXEMPT OFFERINGS MARKET 4
A. Registered Offerings 4
B. The Proliferation of Registration Exemptions 6
1. Exemptions' Salad Days: Private Placements 6
2. Subsequent Developments Regarding the Private Placement Exemption 7
C. Disparity in Investment Access and Calls for Democratization 10
1. Exempt Offerings Operate as the New Norm for Raising Capital 10
2. The Regulatory Structure of Exempt Offerings Creates Unjust Advantages for Elite Investors 12
III. A PROPOSAL: INCLUDE INTRA-INDUSTRY EXPERTS IN THE ACCREDITED INVESTOR DEFINITION 16
A. Recent Movement Toward Democratizing Access for Intra-Industry Experts 16
1. SEC Advisory Committee Recommendations and Subsequent SEC Actions 16
2. Other Calls for Expanding Access to Intra-Industry Experts 19
B. Theoretical and Policy Justifications 21
1. Intra-Industry Experts Can Fend for Themselves 21
2. Intra-Industry Experts Would Facilitate Capital Formation and Promote Economic Performance in the Private Markets 25
IV. MECHANICS OF THE PROPOSAL 28
A. Defining Intra-Industry Expertise 28
1. "Intra-Industry" 28
2. "Expertise" 29
B. Potential Measures to Bolster Investor Protection 31
1. Prior Investment Experience or Financial Knowledge 31
2. Individual Investment Limits 33
3. Supplemental Access of Issuer Information 33
V. CONCLUSION 35

INTRODUCTION

"Every time I look at [this missed investment opportunity], it reminds me of the advice I've been trying to give you all along: Invest in things you know about." – Peter Lynch.[1]

Section 5 of the Securities Act requires that all offers and sales of securities in interstate commerce be registered with the U.S. Securities and Exchange Commission ("SEC" or "Commission") unless an exemption from registration is available.[2] Offerings made pursuant to a registration exemption, commonly referred to as "exempt offerings,"[3] are now more popular than registered offerings.[4] Yet, the number of investors eligible to participate in these exempt offerings remains relatively minuscule.[5] This phenomenon has been criticized for exacerbating economic, social, and political inequalities in the U.S. because only a limited set of privileged investors can access attractive exempt offerings.[6]

In this Article, I propose a method for responsibly expanding investors' access to the exempt offerings market. My proposal concentrates on a class of investors that I refer to as "intra-industry experts," who possess operational or technical expertise regarding an issuer-specific industry. These investors can utilize their knowledge to make well-informed, sophisticated investment decisions. I recommend including intra-industry experts within the definition of accredited investors, an existing category of investors who have substantial access to the private markets via Regulation D.[7]

Part II of this Article provides a broad overview of the history of U.S. capital markets, highlighting the rapid growth of exempt offerings in recent years.

---

1 PETER LYNCH, ONE UP ON WALL STREET: HOW TO USE WHAT YOU ALREADY KNOW TO MAKE MONEY IN THE MARKET 104 (2d ed. 2000).

2 15 U.S.C. § 77e (2011).

3 *See Exempt Offerings*, SEC. & EXCH. COMM'N, https://www.sec.gov/smallbusiness/exempt offerings [https://perma.cc/MEH8-8472] (last modified Feb. 7, 2020).

4 *See* Filipe B. Areno et al., *SEC Adopts Amendments to Exempt Offering Framework*, SKADDEN (Nov. 13, 2020), https://www.skadden.com/insights/publications/2020/11/sec-adopts-amendments-to-exempt-offering-framework [https://perma.cc/68RH-GQAB] (noting how a "robust private market" raised $2.7 trillion in new capital in 2019, compared to just $1.2 trillion raised via registered offerings).

5 SEC. & EXCH. COMM'N, DIV. OF ECON. & RISK ANALYSIS, ACCESS TO CAPITAL AND MARKET LIQUIDITY 43 (2017), https://www.sec.gov/files/access-to-capital-and-market-liquidity-study-2017.pdf [https://perma.cc/9CAE-9RQT] (fewer than 260,000 unique investors likely participated in Regulation D offerings over a seven-year period).

6 *See infra* Part II.C.2.

7 Richard Alsop et al., *SEC Proposes to Update Accredited Investor Definition to Increase Access to Private Investments*, SHEARMAN & STERLING (Jan. 8, 2020), https://www.shearman.com/perspectives/2020/01/sec-proposes-to-update-accredited-investor-definition-to-increase-access-to-private-investments [https://perma.cc/3D47-ZSUK].

This historical background is essential for two reasons. First, it contextualizes this Article's proposal within a trajectory of expanding exempt offering investment opportunities. Second, it supports the underlying democratization rationale of this Article's proposal. As past deregulation of the capital markets has resulted in more companies remaining private longer,[8] companies have increasingly relied on exempt offerings for their capital needs.[9] Part II then details the relationship between the private market's existing structure and income inequality, referencing a robust body of literature on the exacerbating effects of excluding lower-income retail investors from exempt offerings. Part III presents this Article's core proposal of expanding access to exempt offerings for intra-industry experts. It discusses the underlying policy justifications and relevant real-world precedents, including similar recommendations made by private and public sector institutions. Part IV addresses the mechanics for enacting the proposal, including additional investor protection measures that the SEC may employ. Part V concludes with a summary of the Article and recommendations for further research.

II. Evolution of the Exempt Offerings Market

A. Registered Offerings

Registration has historically been the traditional means for offering and selling securities in the U.S. Congress passed the Securities Act of 1933[10] ("Securities Act" or "1933 Act") in response to the market failures of the Great Depression and the consequential public distrust of the stock market.[11] The Exchange Act of 1934 followed thereafter, requiring ongoing public reporting for registered companies.[12] The purpose of the Securities Act was to restore public faith in the markets and prevent fraud in the offer and sale of securities, namely by providing "full and fair disclosure" of the nature and material facts pertaining to those offerings.[13] To that end, it imposed a substantive registration requirement on businesses seeking to raise capital by selling securities.[14]

---

[8] *See generally* Michael Evans & Joan Farre-Mensa, Nat'l Bureau of Econ. Rsch., The Deregulation of the Private Equity Markets and the Decline in IPOs (2019), https://www.nber.org/system/files/working_papers/w26317/w26317.pdf [https://perma.cc/S8GH-NSJS].

[9] *See id.* at 1–2, 8, 15 (finding that the passage of the deregulatory National Securities Markets Improvement Act in 1996 led to increased reliance on Rule 506 of Regulation D to raise capital).

[10] 15 U.S.C. § 77a.

[11] Kenneth Durr & Adrian Kinnane, *431 Days: Joseph P. Kennedy and the Creation of the SEC (1934-35)*, SEC Hist. Soc'y (Dec. 1, 2005), http://www.sechistorical.org/museum/galleries/kennedy/ [https://perma.cc/NF2Q-SRYY].

[12] *See Exchange Act Reporting and Registration*, Sec. & Exch. Comm'n, https://www.sec.gov/smallbusiness/goingpublic/exchangeactreporting [https://perma.cc/CP5B-EXZ3] (last modified Oct. 24, 2018).

[13] SEC v. Ralston Purina Co., 346 U.S. 119, 124, 124 n. 10 (1953).

[14] *Id.* at 124–25.

The Securities Act requires all offers and sales of "securities," as understood within the Act's meaning, to be registered with the SEC or conducted under an exemption from registration.[15] Despite this exempting language, early rulemaking and jurisprudence emphasized the importance of registration. Section 2(a)(1) of the 1933 Act defines a security as "any note, stock, treasury stock, security future, security-based swap, bond, debenture, evidence of indebtedness, … investment contract, …"[16] The Supreme Court deemed this list non-exhaustive,[17] explicitly noting that the definition should be broadly construed.[18] In doing so, the Court adhered to Congress' prophylactic intention to build a broad definition that would include "the many types of instruments that, in our commercial world, fall within the ordinary concept of a security."[19] The Supreme Court later acknowledged this, showing deference to "Congress' purpose in enacting the securities laws []to regulate investments, in whatever form they are made and by whatever name they are called."[20]

The 1933 Act further cast a wide net of applicability in covering *both* the offers and sales of securities. At the heart of this requirement was a public policy concern that issuers might manipulate market performance through selective and well-timed disclosure of offerings.[21] In practice, many feared that initial offering disclosures containing incomplete positive information could condition investors toward participation in the offerings. Issuers could then balance the skewed initial disclosure with negative information provided at the point of sale, depressing investors' reactions to the poorer complete picture.[22] By requiring registration for mere offers of nonexempt transactions, Congress foreclosed the possibility of such market manipulations prior to sales.[23]

Between the breadth of investment vehicles covered by the Act and its application to sales and offers, public offerings were originally considered the primary route to capital raising via securities. However, the expansion of exempt offerings upended the early model of a dominant public capital market.[24]

---

15 15 U.S.C. § 77e(c). *See also* SEC. & EXCH. COMM'N, DIV. OF ECON. & RISK ANALYSIS, *supra* note 5, at 28.

16 15 U.S.C. § 77b(a)(1) (2012).

17 *What Constitutes a Security and Requirements Relating to the Offer and Sales of Securities and Exemptions from Registration Associated Therewith*, A.B.A. (Apr. 27, 2017), https://www.americanbar.org/groups/business_law/publications/blt/2017/04/06_loev/ [https://perma.cc/G6C2-YQG8].

18 SEC v. W. J. Howey Co., 328 U.S. 293, 298–99 (1946) (recognizing that state courts had "broadly construed" the term "investment contract" and holding that it was reasonable to attach that broad understanding to the term as used by Congress).

19 H.R. REP. NO. 85-73, at 11 (1933).

20 Reves v. Ernst & Young, 494 U.S. 56, 61 (1990).

21 Manning Gilbert Warren III, *An Essay on Rule 506 of Regulation D: Its Questionable Origins, Regulatory Oblivion and Judicial Revitalization*, 38 SEC. REG. L.J. 1, 4 (2010).

22 *See id.*

23 *Id.*

24 Elizabeth Pollman, *Private Company Lies*, 109 GEO. L.J. 353, 358 (2020).

B. The Proliferation of Registration Exemptions

1. Exemptions' Salad Days: Private Placements

Issuers can bypass the registration requirements of the 1933 Act if they comply with one of a series of exemptions set forth in Sections 3 and 4 of the Act.[25] At least one such registration exemption has existed since the inception of the Securities Act. The original text of the Securities Act provided an exemption from registration in Section 4(1), later moved to Section 4(2) via revisions to the Securities Act in 1964, for "transactions by an issuer not involving any public offering."[26] This exemption remains in effect,[27] having been moved most recently to Section 4(a)(2) of the Securities Act via the JOBS Act of 2012.[28] It is commonly referred to as the "private offering" exemption.[29]

Historical records demonstrate that companies utilized this exemption immediately after the Securities Act went into effect. Between the years 1934–1940, a total of 848 transactions bypassed registration under this exemption.[30] These transactions, referred to at the time as "direct purchases,"[31] accounted for 23% of the total dollar amount raised by issuers during the corresponding period.[32] Exempt offerings under 2(a)(10) increased in popularity during that six- or seven-year period as measured across various criteria, including total number of exempt

---

[25] JAMES D. COX, ROBERT W. HILLMAN & DONALD C. LANGEVOORT, SECURITIES REGULATION: CASES AND MATERIALS 239 (9th ed. 2020).

[26] Stuart R. Cohn, *Securities Markets for Small Issuers: The Barrier of Federal Solicitation and Advertising Prohibitions*, 38 U. FLA. L. REV. 1, 2 n. 4 (1986).

[27] 15 U.S.C. § 77d(a)(2) (2012).

[28] *Section 4(a)(2)*, THOMSON REUTERS: PRAC. L., https://1.next.westlaw.com/6-382-3799 [https://perma.cc/YH4L-9XN6] (last accessed Nov. 23, 2021).

[29] *See, e.g.*, SEC v. Ralston Purina Co., 346 U.S. 119, 122 (1953).

[30] *Proposed Amendments to the Securities Act of 1933 and to the Securities Exchange Act of 1934: Hearings Before the H. Comm. On Interstate and Foreign Commerce on a Comparative Print Showing Proposed Changes in the Securities Act of 1933 and the Securities Exchange Act of 1934 and H.R. 4344, H.R. 5065, and H.R. 5832*, 77th Cong. 366 (1941), https://books.google.com/books?id=Q4TpAAAAMAAJ&pg=PA366 [https://perma.cc/VUJ4-AVUE] [hereinafter *Proposed Amendments*]. A more legible digitized copy of this data is available via the SEC Historical Society. SEC HIST. SOC'Y, CORPORATE SECURITIES SOLD IN TRANSACTIONS EXEMPTED FROM SECURITIES ACT REGISTRATION AS NOT INVOLVING ANY "PUBLIC OFFERING" 3 tbl.C (1941), http://www.sechistorical.org/collection/papers/1940/1941_0915_SecuritiesExempted. pdf [https://perma.cc/KQ6U-RLNS].

[31] *See Proposed Amendments, supra* note 30, at 364–65.

[32] *Id.* at 366 tbl.D.

issuances,[33] total dollars raised via exempt issuances,[34] and the proportion of total dollars raised via direct purchases.[35]

Even with such usage, issuers struggled with statutory ambiguities and practical confusion regarding the private offering exemption.[36] The Securities Act failed to define a "public offering" and establish the boundaries of private offerings, and legislative history provides little elucidation.[37] To the minimal extent that legislative history addresses the underlying rationale or supposed merits of this exemption, Congress viewed it as covering transactions "where there is no particular need for [the Act's] application or where the public benefits [of registration] are too remote."[38] In considering the rationale of exemptions more broadly, legislative history also reflects a general desire to avoid unnecessary burdens on "legitimate transactions."[39]

2. Subsequent Developments Regarding the Private Placement Exemption

Following the 1933 Act, the SEC entered "an almost constant state of experimentation" in the area of registration exemptions,[40] with additional contributions by the judiciary.[41] With a steady stream of clarifications regarding the private placement exemption and rules building upon it, the next half-century represented a trend toward more workable registration exemptions.[42] This aligned

---

[33] 393 exempt offerings were conducted under 2(a)(10) in 1940, as opposed to 12 in 1934 and 135 in 1939. *Id*. at 373 tbl.C.

[34] Companies raised $1.5 billion via exempt offerings conducted under 2(a)(10) in 1940, as opposed to $96 million in 1934 and $827 million in 1939. *Id.* at 365 tbl.A.

[35] "Direct purchases" accounted for 43.59% of total dollar financing in 1940, as opposed to 16.68% in 1934 and 34% in 1939. *Id.* at 366 tbl.D.

[36] *See, e.g.*, *Proposed Amendments*, *supra* note 30, at 363–65 (statement of R. McLean Stewart, Chairman, Securities Acts Committee, Investment Bankers' Association of America) (emphasizing the incongruity between the expected limited scope of private offerings and the volume of transactions covered by the exemption).

[37] SEC v. Ralston Purina Co., 346 U.S. 119, 122 (1953).

[38] H.R. REP. NO. 85-73 at 5 (1933).

[39] *To Provide for The Furnishing of Information and the Supervision of Traffic in Investment Securities in Interstate Commerce: Hearing on H.R. 4314 Before the H. Comm. on Banking and Currency*, 73d Cong. 332 (1933), https://books.google.com/books?id=8VNBAQAAIAAJ&pg=PA332 [https://perma.cc/QUG3-YX4R] (embedded report entitled A STUDY OF THE ECONOMIC AND LEGAL ASPECTS OF THE PROPOSED FEDERAL SECURITIES ACT) ("One of the important problems in this type of legislation concerns exemptions from its provisions. These should be chosen with a view to embodying the least possible burden on legitimate transactions without, at the same time, providing means for evasion of the law's restraining clauses by fraudulent manipulators.").

[40] Mark A. Sargent, *The New Regulation D: Deregulation, Federalism and the Dynamics of Regulatory Reform*, 68 WASH. U. L.Q. 225, 236 (1990), https://openscholarship.wustl.edu/cgi/viewcontent.cgi?article=1944&context=law_lawreview [https://perma.cc/ZYP2-2H99].

[41] *See infra* Part II.B.2.

[42] Sargent, *supra* note 40, at 237.

with an increasing broader societal preference for deregulation, culminating with the Reagan Administration.[43]

In 1935, the SEC developed a four-factor test to determine what transactions were private and thus did not need to be registered.[44] Despite this clarification, proposals to amend the Securities Act in 1941 and 1947 focused on changing the registration and prospectus requirements of the Act.[45] Specifically, one amendment proposal sought to rectify the ambiguity surrounding the private offerings exemption by providing a statutory definition of "public offering."[46] However, this amendment proposal was not adopted before the Supreme Court weighed in on the matter.[47]

In 1953, the Supreme Court in *SEC v. Ralston Purina Co.*[48] sought to define the scope of the private offering exemption.[49] Ralston Purina, a manufacturer and distributor of agricultural products, offered treasury stock to its "key employees" and sought the private offering exemption of Section 4(a)(2) (then Section 4(1)) to avoid registration with the SEC.[50] The Court held that exemptions apply to securities transactions in which the participants do not need the protections of the 1933 Act's registration requirements.[51] It articulated two characteristics that characterize such transactions: (1) the offerees are those "able to fend of

---

[43] *Id.* at 237–38. From a macro perspective, the decades following President Franklin D. Roosevelt's New Deal strengthening of federal agencies can be considered a period of reactive deregulation. Susan Dudley, *A Brief History of Regulation and Deregulation*, REG. REV. (Mar. 11, 2019), https://www.theregreview.org/2019/03/11/dudley-brief-history-regulation-deregulation/ [https://perma.cc/H4LL-B2VW]. Critics have noted deregulation as one of the stand-out features of the Reagan Administration. *See, e.g.*, Paul Krugman, *Reagan Did It*, N.Y. TIMES (May 31, 2009), https://www.nytimes.com/2009/06/01/opinion/01krugman.html [https://perma.cc/A2HV-FQVK]; Frank Swoboda, *The Legacy of Deregulation*, WA. POST (Oct. 2, 1988), https://www.washingtonpost.com/archive/business/1988/10/02/the-legacy-of-deregulation/c553674b-8bd2-436e-9be7-7de95f798fbb/ [https://perma.cc/S3CB-E4SN].

[44] Factors Involved in Determining Whether Transaction is "Public Offering," Securities Act Release No. 33-285, Fed. Sec. L. Rep. (CHH) ¶ 2740 (Jan. 24, 1935) (identifying the four factors as the number of offerees, relationship of the offerees to each other and to the issuer, number of units offered, and size of the offering).

[45] Clark Byse & Raymond J. Bradley, *Proposals to Amend the Registration and Prospectus Requirements of the Securities Act of 1933*, 96 U. PENN. L. REV. 609, 609 (1948).

[46] *Proposed Amendments, supra* note 30, at 363.

[47] Had the proposal been adopted, it would not have been the case that "public offering" was undefined statutorily by the time of the Ralston Purina opinion in 1953. *See* SEC v. Ralston Purina Co., 346 U.S. 119, 122 (1953). Indeed, the phrase remains undefined statutorily at the time of writing. Facilitating Capital Formation, Securities Act Release No. 10763, Exchange Act Release No. 88321, Fed. Sec. L. Rep. (CCH) ¶ 82,546, at 62 (Mar. 4, 2020), https://www.sec.gov/rules/proposed/2020/33-10763.pdf [https://perma.cc/XR6T-S4MA] (Proposing Release) [hereinafter *Proposing Release No. 10763*].

[48] 346 U.S. 119 (1953).

[49] *Id.* at 120.

[50] *Id.*

[51] *Id.* at 125.

themselves"[52] (a quality often referred to as sophistication),[53] and (2) the offerees have access to similar information in the exempt offering as they would have in a registered offering.[54] In essence, the Court sought to restrict exempt offerings to those investors who "know what they don't know and know how to ask" for additional information.[55]

Subsequent private placement litigation has largely focused on identifying the offerees who require the protections afforded by registration and thus are ineligible participants under Section 4(a)(2).[56] One of the most elusive issues in the case law is how to define sophistication, which many courts simply avoid addressing.[57] Even beyond the nebulous standard of sophistication, courts have yet to fully explain an appropriate process by which an issuer can measure a prospective offeree's sophistication.[58]

In the years following *Ralston Purina*, the use of the private offering exemption expanded dramatically to include widespread selling of speculative securities to wealthy individuals.[59] Ten years after the Court's decision, the SEC issued Release No. 4552.[60] Noting the "increasing tendency to rely upon the exemption for offerings of speculative issues to unrelated and uninformed persons," the SEC sought to clarify the parameters of the exemption.[61] It acknowledged that Section 4(a)(2) determinations lack a bright-line rule, depending instead on a multi-factor facts and circumstances analysis.[62] The factors included the nature, scope, size, type and manner of the offering.[63] Release No. 4552 also addressed integration determinations for exempt offerings, though commentators have noted the problematic nature of such guidance.[64]

---

52 *Id.*

53 *See, e.g.*, COX, HILLMAN & LANGEVOORT, *supra* note 25, at 245.

54 Ralston Purina Co., 346 U.S. at 125, 127.

55 Urska Velikonja & J. W. Verret, *Deep Dive Episode 38 – The Debate Over the SEC's Accredited Investor Standard*, REG. TRANSPARENCY PROJECT: FOURTH BRANCH PODCAST, at 19:30 (Feb. 6, 2019), https://regproject.org/podcast/deep-dive-ep-38/ [https://perma.cc/TA5J-CUZL].

56 COX, HILLMAN & LANGEVOORT, *supra* note 25, at 245 (discussing the effect that *Ralston Purina* had on numerical guidelines, including a pre-existing rule of thumb that limited private offerings to 25 or fewer offerees).

57 *Id.* at 250.

58 *Id.*

59 Tom A. Alberg & Martin E. Lybecker, *New SEC Rules 146 and 147; The Nonpublic and Intrastate Offering Exemptions from Registration for the Sale of Securities*, 74 COLUM. L. REV. 622, 625 (1974), https://www.jstor.org/stable/pdf/1121723.pdf [https://perma.cc/477L-J8EN].

60 Nonpublic Offering Exemption, Securities Act Release No. 33-4552, Fed. Sec. L. Rep (CCH) ¶ 2770 (Nov. 6, 1962), https://www.sec.gov/rules/final/33-4552.htm [https://perma.cc/B88A-YC99].

61 *Id.*

62 *Id.*

63 *Id.*

64 COX, HILLMAN & LANGEVOORT, *supra* note 25, at 313.

Next, the SEC adopted Rule 146,[65] in an effort to address issuers' uncertainty with the legal framework surrounding the private offering exemption and need for objective standards.[66] Crucially, Rule 146 attempted to clearly define the dual characteristics of sophistication and access to information first articulated in *Ralston Purina*.[67] It stated that investors were financially sophisticated enough to participate in private placement transactions based on their knowledge and experience, capability of evaluating the risk and merits, and ability to bear the economic risk of investment.[68]

Despite the multiple attempts by the courts and SEC to clarify the contours of the private placement exemption, small business issuers lobbied the SEC to adopt a more objective standard and predictable framework for exempt offerings.[69] A critical component of this lobbying effort was pressuring the SEC to shift the basis of exempt offerings from investor sophistication to a wealth standard.[70] In response, the SEC promulgated Regulation D in 1982, aiming to reduce regulatory constraints on capital formation.[71] Regulation D vastly expanded opportunities for investors to participate in the private markets by utilizing the new "accredited investor" standard, under which qualifying investors enjoyed a presumption of sophistication.[72]

C. Disparity in Investment Access and Calls for Democratization

1. Exempt Offerings Operate as the New Norm for Raising Capital

As the avenues to raise capital through exempt offerings have grown,[73] the exempt securities markets have also grown in popularity, both in terms of absolute amounts raised and in relation to registered offerings.[74] In 2019, exempt offerings accounted for approximately $2.7 trillion of new capital raising, representing

---

65 Adopted in Securities Act Release No. 5487 (Apr. 23, 1974).

66 Alberg & Lybecker, *supra* note 59, at 632.

67 *Id.* at 634.

68 U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-13-640, SECURITIES AND EXCHANGE COMMISSION: ALTERNATIVE CRITERIA FOR QUALIFYING AS AN ACCREDITED INVESTOR SHOULD BE CONSIDERED 8 (2013), http://www.gao.gov/assets/660/655963.pdf [https://perma.cc/9P3Z-KJCW].

69 Jennifer J. Johnson, *Private Placements: A Regulatory Black Hole*, 35 DEL. J. CORP. L. 151, 168 (2010).

70 Velikonja & Verret, *supra* note 55, at 19:35.

71 Sargent, *supra* note 40, at 227.

72 *See* Syed Haq, *Revisiting the Accredited Investor Standard*, 5 MICH. BUS. & ENTREPRENEURIAL L. REV. 59, 62–63 (2016) (describing the effect of Regulation D in enabling issuers to "raise a virtually indefinite amount of funds through a limitless pool of purchasers, as long as they were accredited investors."). For the precise parameters of exempt offerings conducted pursuant to Rules 504, 505, and 506 of Regulation D, *see* 17 C.F.R. §§ 230.504-06 (2015); *infra* Part II.C.2.

73 *See supra* Part II.B.

74 *Proposing Release No. 10763*, *supra* note 47, at 8.

nearly 70% of the total securities markets.[75] Conversely, issuers raised just $1.2 trillion, or 30%, through public registered offerings.[76] The heightened activity in exempt offerings markets may be even more pronounced than the numbers suggest, as there is minimal data regarding the largest segment of the private market—Regulation D.[77]

The reason why issuers gravitate toward exempt offerings lies, at least in part, in the recent discourse concerning companies' collective preference to remain private longer.[78] Typically, a company becomes subject to a complex regulatory process once it registers with the SEC to sell securities pursuant to the 1933 Act.[79] J.W. Verret posits that issuers' decisions to rely on exempt offerings for capital formation, and by extension abstain from going public, come down primarily to the direct costs associated with being a public company. Such costs include compliance with the Sarbanes-Oxley Act ("SOX") generally, SOX Section 404(b) internal controls certification requirements, securities litigation, shareholder proposals, proxy advisors, and various other corporate governance requirements.[80] Additionally, firms may avoid registration in order to reduce the likelihood of unintentional violations of 1933 Act rules.[81] Remaining private also limits

---

[75] *Id.* These figures are based on analyses by the Commission's Division of Economic and Risk Analysis ("DERA") via data collection from SEC filings. *Id.* at 8 n. 12.

[76] *Id.*

[77] *See* Allison Herren Lee, *Statement on Amendments to the Exempt Offering Framework*, SEC. & EXCH. COMM'N (Nov. 2, 2020), https://www.sec.gov/news/public-statement/lee-harmonization-2020-11-02 [https://perma.cc/229G-828R].

[78] *See, e.g.*, Allison Herren Lee, *Going Dark: The Growth of Private Markets and the Impact on Investors and the Economy*, SEC. & EXCH. COMM'N (Oct. 12, 2021), https://www.sec.gov/news/speech/lee-sec-speaks-2021-10-12 [https://perma.cc/X3S4-QJ5G]; Velikonja & Verret, *supra* note 55, at 7:10 (noting how exempt offerings markets relate to issuers' increasing preference to stay private); *Staying Private Longer: Why Go Public?*, A.B.A. (Sept. 13, 2019), https://www.americanbar.org/groups/business_law/resources/materials/2019/annual_materials/staying_private/ [https://perma.cc/LU9B-H5FH] ("Thus, given the abundance of private capital available, companies no longer require public markets for sufficient funding."); Begum Erdogan et al., *Grow fast or die slow: Why unicorns are staying private*, MCKINSEY (May 11, 2016), https://www.mckinsey.com/industries/technology-media-and-telecommunications/our-insights/grow-fast-or-die-slow-why-unicorns-are-staying-private [https://perma.cc/TD9X-3R4V].

[79] Stuart Evan Smith, *The Securities and Exchange Commission's Proposed Regulations under the CROWDFUND Act Strike a Necessary Balance between the Burden of Disclosure Placed on Issuers of Securities and Meaningful Protection for Unsophisticated Investors*, 44 U. BALT. L. REV. 127, 136 (2014); Caroline Banton, *Public Company*, INVESTOPEDIA (Jan. 20, 2021), https://www.investopedia.com/terms/p/publiccompany.asp [https://perma.cc/U4AN-UJ7J] ("A company is required to conform to public reporting requirements once they meet any of these criteria: Sell securities in an initial public offering (IPO)[, t]heir investor base reaches a certain size[, or they v]oluntarily register with the SEC.").

[80] Velikonja & Verret, *supra* note 55, at 7:45.

[81] *Id.* at 10:30.

companies' public disclosure of information, which competitors might otherwise use to their advantage.[82]

Issuers' concerns regarding registration are meritorious. Issuers must pay a base fee to register securities with the SEC,[83] which currently charges $92.70 for every $1 million raised through the offering.[84] Firms incur additional related expenses, such as accounting and legal fees, when registering.[85] In aggregate, filing costs associated with registration can be as much as $100,000 even for a small offering.[86] PricewaterhouseCoopers' online calculator estimates the average cost directly attributable to an initial public offering (IPO) to total millions of dollars.[87] Beyond the initial registration fees, firms incur ongoing costs associated with being public. In a 2011 report, the IPO Task Force found that regulatory compliance for an IPO costs an average of $2.5 million initially, followed by an average ongoing compliance cost of $1.5 million annually.[88] These figures help explain both the growth in capital raising through exempt offerings[89] and the rising trend of companies opting to forego public status.[90]

2. The Regulatory Structure of Exempt Offerings Creates Unjust Advantages for Elite Investors

The dominance of the exempt offerings market catalyzed scholarly and regulatory attention toward democratizing access for retail investors to potentially high-growth private companies.[91] Securities law expert Donald Langevoort noted one "alarming" trend: as companies are increasingly economically incentivized to stay private, public equity becomes a less available investment opportunity for

---

[82] René M. Stulz, *Public Versus Private Equity*, HARV. L. SCH. F. CORP. GOVERNANCE (Mar. 23, 2020), https://corpgov.law.harvard.edu/2020/03/23/public-versus-private-equity/ [https://perma.cc/ZRT5-LVEP].

[83] *Fee Rate Advisory #1 for Fiscal Year 2021*, SEC. & EXCH. COMM'N (Aug. 26, 2020), https://www.sec.gov/news/press-release/2020-196 [https://perma.cc/N7AH-XFZL].

[84] *Filing Fee Rate*, SEC. & EXCH. COMM'N, https://www.sec.gov/ofm/Article/feeamt.html [https://perma.cc/Q98T-UXBP] (last modified Oct. 1, 2021).

[85] Smith, *supra* note 79, at 136.

[86] *Id.*

[87] *See Considering an IPO? First, Understand the Costs*, PWC, https://www.pwc.com/us/en/services/deals/library/cost-of-an-ipo.html [https://perma.cc/MQ29-3SFT] (last accessed Nov. 23, 2021).

[88] IPO TASK FORCE, REBUILDING THE IPO ON-RAMP: PUTTING EMERGING COMPANIES AND THE JOB MARKET BACK ON THE ROAD TO GROWTH 9 (2011), https://www.sec.gov/info/smallbus/acsec/rebuilding_the_ipo_on-ramp.pdf [https://perma.cc/3BW3-RFSJ].

[89] *Proposing Release No. 10763*, *supra* note 47, at 8.

[90] See. Phil Mackintosh, *The Battle for Public vs Private Equities,* NASDAQ (Feb. 27, 2020, 1:33 PM), https://www.nasdaq.com/articles/the-battle-for-public-vs-private-equities-2020-02-27 [https://perma.cc/T3KH-8L4J].

[91] Pollman, *supra* note 24, at 359.

retail investors.[92] Increasing concentration of equity in the hands of wealthy, elite investors has had both deleterious economic and political effects.[93]

Exempt offerings provide investors with significant advantages over registered offerings.[94] Evidence suggests that private market offerings outperform their public counterparts as higher returns and lower agency costs are associated with exempt offering investments.[95] Furthermore, unregistered securities enjoy lower volatility, likely due to their illiquid nature.[96] These advantages may explain why private companies' valuations have risen so dramatically in recent years.[97]

The unfortunate reality of private capital markets' structure is that the bulk of economic benefits derived from exempt offerings are, by definition, restricted to elite investors. To understand how this came to bear, one must first understand the enabling regulatory structure, particularly as it pertains to Regulation D. In recent years, Regulation D has become the most preferred method of capital raising relative to both registered offerings and other exempt offerings.[98] Rule 506 offerings account for approximately 99.9% of capital raised through Regulation D.[99] Although Regulation D allows both accredited and non-accredited investors to participate in the exempt offerings, Rule 506(b) offerings allow only 35 non-accredited investors, and Rule 506(c) excludes them altogether.[100] Even if an issuer decides to conduct a Rule 506(b) offering, any non-accredited investors hoping to

---

92 DONALD C. LANGEVOORT, SELLING HOPE, SELLING RISK: CORPORATIONS, WALL STREET, AND THE DILEMMAS OF INVESTOR PROTECTION 165 (2016).

93 *See, e.g.*, Mackintosh, *supra* note 90 (summarizing several key economic and social policy arguments for democratizing access to investment opportunities).

94 Kevin G. Bender, *Giving the Average Investor the Keys to the Kingdom: How the Federal Securities Laws Facilitate Wealth Inequality*, 15 J. BUS. & SEC. L. 1, 14–25 (2016).

95 *Everyone Now Believes That Private Markets Are Better Than Public Ones*, ECONOMIST (Jan. 30, 2020), https://www.economist.com/finance-and-economics/2020/01/30/everyone-now-believes-that-private-markets-are-better-than-public-ones [https://perma.cc/D2RK-96VD] (noting the economic benefits of private market investments while cautioning investors against blind faith in private offerings).

96 EQUISAFE, *Private Markets and Public Markets*, MEDIUM (June 9, 2020), https://medium.com/@Equisafe/private-markets-and-public-markets-56450eca352e [https://perma.cc/VY4T-VYAM].

97 David F. Larcker et al., *Cashing It In: Private-Company Exchanges and Employee Stock Sales Prior to IPO*, HARV. L. SCH. F. CORP. GOVERNANCE (Oct. 9, 2018), https://corpgov.law.harvard.edu/2018/10/09/cashing-it-in-private-company-exchanges-and-employee-stock-sales-prior-to-ipo/ [https://perma.cc/K3FK-WHVZ]. One recent study shows post money, pre-IPO valuations for high-growth technology companies to have increased from an average of $17 billion in 2015 to $92 billion in 2020. Gené Teare, *Unicorns Get More Magical: 2020 Cohort Shows Huge Increase in Valuation on IPO Day*, CRUNCHBASE (Nov. 2, 2020), https://news.crunchbase.com/news/unicorns-get-more-magical-2020/ [https://perma.cc/7SER-KBYS].

98 SCOTT W. BAUGUESS ET AL., SEC. & EXCH. COMM'N, DIV. OF ECON. & RISK ANALYSIS, CAPITAL RAISING THE U.S.: AN ANALYSIS OF THE MARKET FOR UNREGISTERED SECURITIES OFFERINGS, 2009-2017 5, 7–8, 8 FIG. 1 (2018), https://www.sec.gov/files/DERA%20white%20paper_Regulation%20D_082018.pdf [https://perma.cc/XWL2-L5JX].

99 *Id.* at 13–14.

100 *Id.* at 34.

participate must be "sophisticated," a requirement which has led Rule 506(b) issuers to almost always exclude non-accredited investors.[101]

Rule 501(a) of Regulation D enumerates the classes of individuals and institutions that may qualify as accredited investors.[102] Prior to recent amendments by the SEC,[103] the accredited investor definition, and by extension individual investors' access to private capital markets, was largely "rooted in income and wealth tests."[104] As noted by Kevin G. Bender, "All the private offering exemptions share one significant requirement: they restrict investment participation to specific high income and high net-worth individuals through, in the case of the Securities Act, the accredited investor standard."[105]

From an economic and social policy perspective, commentators criticized these income and wealth tests for their exclusionary effect on lower income Americans. Critics emphasized the tests' exacerbating effects on wealth and income inequality.[106] Former SEC Chairman Jay Clayton appeared to agree with these criticisms, stating in an interview with CNBC's Andrew Ross Sorkin, "If the growth opportunities have shifted—not all the way, but to a substantial extent—into our private markets and ordinary investors don't have access to them, that's not good."[107]

These are valid concerns. The effective gatekeeping that preserves private offerings primarily for wealthy investors disadvantages retail investors and

---

[101] *Id.* at 35 (only seven percent of Rule 506(b) offerings from 2009–2017 included or intended to include nonaccredited investors).

[102] 17 CFR § 230.501 (a)(1)-(13).

[103] *See infra* Part II.

[104] Jay Clayton, Chairman, Sec. & Exch. Comm'n, Remarks to the Economic Club of New York (Sept. 9, 2019), https://www.sec.gov/news/speech/speech-clayton-2019-09-09 [https://perma.cc/RHJ8-9GM9]. The relevant net worth and income tests are presented in 17 CFR 230.501 (a)(5)-(6).

[105] Bender, *supra* note 94, at 8.

[106] *See, e.g.*, Frank Holmes, *The Barriers To Investing In Private Equity Are Too High*, FORBES (Oct. 15, 2019, 4:22 PM EDT), https://www.forbes.com/sites/greatspeculations/2019/10/15/the-barriers-to-investing-in-private-equity-are-too-high/ [https://perma.cc/8UHT-ZZV9] ("The rich are getting richer and the poor are getting poorer, and for that we can largely blame policies of envy that increasingly restrict investors' access to wealth-building instruments."); John Berlau, *Let Middle-Class Investors Join the 'Accredited' Club*, COMPETITIVE ENTERPRISE INST. (Aug. 27, 2018), https://cei.org/opeds_articles/let-middle-class-investors-join-the-accredited-club/ [https://perma.cc/JPP9-4XUF] ("[Because of the accredited investor income and wealth tests,] only wealthy Americans have the opportunity to grow even wealthier with the startup that could become the next Uber or Facebook.").

[107] *CNBC Exclusive: CNBC's Andrew Ross Sorkin Interviews United States Securities And Exchange Commission Chairman Jay Clayton From CNBC Institutional Investor Delivering Alpha Conference*, CNBC (Sept. 19, 2019, 11:24 AM EDT), https://www.cnbc.com/2019/09/19/cnbc-exclusive-cnbcs-andrew-ross-sorkin-interviews-united-states-securities-and-exchange-commission-chairman-jay-clayton-from-cnbc-institutional-investor-delivering-alpha-conference.html [https://perma.cc/69MB-LHW3].

facilitates wealth inequality.[108] Retail investors' investment options in the public markets lack the stability and trading strategy flexibility characterized by their private market counterparts.[109] Furthermore, retail investors have relatively poor portfolio diversification and, by extension, risk optimization instruments due to being shut out of the private markets.[110] As private equity investments outperform investments in the public markets across both the short and long-term,[111] the wealth gap between accredited and non-accredited investors stands to grow.[112] Given recent recognition of rising income and wealth inequality in the U.S.,[113] responsibly reducing the barriers to access the private markets bears the flag of economic justice.[114]

Democratizing access to private markets may also have political effects. Amy Deen Westbrook and David A. Westbrook contextualized retail investors' participation in capital markets as a core feature of cultural value and republican capitalism.[115] They argue that the dramatic shift of economic activity toward private markets, from which retail investors are excluded, has reimagined what the "stock market" means as a matter of political economy and has fomented, at least in part, populist discontent over economic conditions.[116] Broader economic and political trends suggest a practical connection between wealth and income inequality and political change,[117] lending credence to Westbrook & Westbrook's

---

[108] For a detailed articulation of this claim and the subsequent points, see Bender, *supra* note 94, at 25–41.

[109] *Id.* at 25.

[110] *Id.* at 34.

[111] *New Report: Private Equity Outperforms Public Markets Across the Short and Long-Term*, AM. INV. COUNCIL (Sept. 18, 2018), https://www.investmentcouncil.org/new-report-private-equity-outperforms-public-markets-across-the-short-and-long-term/ [https://perma.cc/VV2F-75JL]. *Contra* Bender, *supra* note 94, at 34 ("Although pubic [sic] stock markets tend to post the highest average annual returns, they also come with the most risk.").

[112] *See generally* Marcin Kacperczyk et al., *Investor Sophistication and Capital Income Inequality*, 107 J. MONETARY ECON. 18 (2019) (finding capital income inequality exists and is increasing between sophisticated and unsophisticated investors). Like the "accredited investor" definition of Regulation D, the study equates wealth with sophistication. *Id.* at 25 ("We classify as sophisticated investors the participants in the top decile of the wealth distribution, and relatively unsophisticated investors as the remaining 90% of participants.").

[113] *See, e.g.*, Julia Menasce Horowitz et al., *1. Trends In Income And Wealth Inequality*, PEW RES. CTR (Jan. 9, 2020), https://www.pewresearch.org/social-trends/2020/01/09/trends-in-income-and-wealth-inequality/ [https://perma.cc/GB5Y-9D9B] ("Economic inequality, whether measured through the gaps in income or wealth between richer and poorer households, continues to widen.").

[114] *See* Bender, *supra* note 94, at 41 ("The public policy of our securities laws should be to promote market fairness and efficiency, not facilitate economic disparity.").

[115] Amy Deen Westbrook & David A. Westbrook, *Unicorns, Guardians, and the Concentration of the U.S. Equity Markets*, 96 NEB. L. REV. 688, 690 (2018).

[116] *Id.*

[117] Catherine Kress, *The Economics of Social Unrest*, BLACKROCK (Feb. 11, 2020), https://www.blackrock.com/us/individual/insights/the-economics-of-social-unrest [https://perma.cc/YSA5-SNUH].

theory. Others have argued that the existing legal structure surrounding the accredited investor definition and access to private markets exacerbates racial inequality, and still others have noted the similarities between private market access restrictions and historical race-based prohibitions.[118]

III. A PROPOSAL: INCLUDE INTRA-INDUSTRY EXPERTS IN THE ACCREDITED INVESTOR DEFINITION

The second Part of this Article illustrates how unregistered offerings progressively became the dominant means of capital formation in the U.S. It also demonstrates that consequentially, securities law structurally exacerbates broader inequalities by unfairly limiting less-wealthy investors from accessing exempt offerings. To address this problem, securities law should welcome opportunities to responsibly expand access to private markets for investors who are capable of fending for themselves. One such opportunity is facilitating private market participation by intra-industry experts—investors with operational or technical sophistication regarding the issuer's industry. This Part highlights prior calls for and examples of comparable regulatory innovation. It then outlines the theoretical and policy justifications for its proposal.

A. Recent Movement Toward Democratizing Access for Intra-Industry Experts

1. SEC Advisory Committee Recommendations and Subsequent SEC Actions

This Article's proposal to exempt offers and sales of securities to intra-industry experts is not novel. In fact, prominent individuals and organizations, including voices close to the SEC, have independently endorsed the concept in recent years. At the forefront of such efforts has been the SEC Advisory Committee

---

118 *See, e.g.*, Mariah Lichtenstern, *Investors Still Engage in Racist Redlining. Why Haven't We Done Something About It?*, FORTUNE (Jan. 6, 2021, 7:00 PM EST), https://fortune.com/2021/01/06/redlining-black-latinx-entrepreneurship-investment-sec/ [https://perma.cc/2DC2-P6UK] ("The accredited investor rule needs to change because it reinforces the racial wealth gap and perpetuates income inequality. The laws as they stand are one more vestige of systemic racism we need to eradicate."); Arlan Hamilton & Molly Wood, *It Takes Money To Make Money — That's An Actual Regulation*, MARKETPLACE: MARKETPLACE TECH (Oct. 28, 2020), https://www.marketplace.org/shows/marketplace-tech/private-equity-accredited-investor-securities-and-exchange-commission-racial-wealth-gap/ [https://perma.cc/6XV9-58VC]; Leah Duncan, *Arbitrary Paternalism and the SEC Accredited-Investor Standard*, MICH. J. RACE & L. (Dec. 4, 2018), https://mjrl.org/2018/12/04/arbitrary-paternalism-and-the-sec-accredited-investor-standard/ [https://perma.cc/RF3E-BYUV].

on Small and Emerging Companies ("the Committee"),[119] now organized as the SEC Small Business Capital Formation Advisory Committee.[120] In 2015, the Committee advocated for expanding the accredited investor definition to cover those investors who meet a "sophistication test," without consideration for the traditional income or net worth assessments.[121]

The following year, the Committee authored an additional report on the accredited investor definition which speaks directly to this Article's proposal.[122] First, whereas the accredited investor definition traditionally relied upon financial thresholds of wealth and net worth, the Committee suggested expanding the definition to "take into account measures of non-financial sophistication."[123] Second, it called on the SEC to explore including investors who would not otherwise be considered accredited and possess "specific industry or issuer knowledge or expertise."[124] With these recommendations, the Committee sought to expand the pool of accredited investors, arguing that expansion comports with a "do no harm" approach to the private offering ecosystem.[125]

The Committee debate concerning the 2016 report is especially enlightening. Committee members described how including intra-industry experts in the accredited investor definition would support private market democratization efforts.[126] Additionally, they explained how intra-industry experts are sufficiently

---

[119] *Spotlight on Advisory Committee on Small and Emerging Companies*, SEC. & EXCH. COMM'N, https://www.sec.gov/spotlight/advisory-committee-on-small-and-emerging-companies.shtml [https://perma.cc/2MQ4-PPT7] (last modified Nov. 25, 2019).

[120] *Small Business Capital Formation Advisory Committee*, SEC. & EXCH. COMM'N, https://www.sec.gov/page/small-business-capital-formation-advisory-committee [https://perma.cc/3K6W-H8KR] (last modified Nov. 15, 2021) ("The Committee succeeds the SEC's former Advisory Committee on Small and Emerging Companies, whose term expired in 2017.").

[121] ADVISORY COMM. SMALL & EMERGING COS., SEC. & EXCH. COMM'N, RECOMMENDATIONS REGARDING THE ACCREDITED INVESTOR DEFINITION 3 (2015), https://www.sec.gov/info/smallbus/acsec/acsec-accredited-investor-definition-recommendation-030415.pdf [https://perma.cc/L9EW-NJE4] [hereinafter *2015 Report*].

[122] *See generally* ADVISORY COMM. SMALL & EMERGING COS., SEC. & EXCH. COMM'N, RECOMMENDATIONS REGARDING THE ACCREDITED INVESTOR DEFINITION (2016), https://www.sec.gov/info/smallbus/acsec/acsec-recommendations-accredited-investor.pdf [https://perma.cc/4ER2-4MMQ] [hereinafter *2016 Report*].

[123] *Id.* at 2.

[124] *Id.*

[125] Transcript of Proceedings of the U.S. Sec. & Exch. Comm'n Advisory Comm. On Small & Emerging Cos., at 15 (July 19, 2016, 9:31am), https://www.sec.gov/info/smallbus/acsec/acsec-transcript-071916.pdf [https://perma.cc/5Z4L-M744] [hereinafter *2016 Proceedings*] (remarks by Co-Chair Hanks); *2015 Report*, *supra* note 121, at 3.

[126] *See, e.g.*, *2016 Proceedings*, *supra* note 125, at 30 ("[I]t's also equally and maybe more important that we're giving our people the opportunity at the broadest possible section to invest in the United States and in their small companies.") (comment by Ms. Yamanaka); *id.* at 41 ("[I]t seems a little bit out of bounds when we start trying to protect people from themselves as opposed to trying to protect people from fraudsters when—because you come from a certain background or a certain income level you're not given the opportunity to invest in things that could be very lucrative.")

differentiated from ordinary retail investors and how intra-industry expertise supports investment sophistication.[127] Although the final recommendation does not clearly articulate what constitutes "specific industry or issuer knowledge or expertise" to qualify for accredited investor status,[128] Committee Co-Chair Sarah Hanks summarized it as an attempt at formulating a rule embodying the "invest in what you know" maxim.[129]

The SEC responded to these calls, among others,[130] by adopting amendments to the accredited investor definition.[131] These amendments granted accredited investor status to natural persons with certain professional certifications, primarily those directly associated with the securities and investment industries, knowledgeable employees of private funds, and others.[132] Although the revised definition was limited to expanding opportunities for those professionally involved in the securities and investment industry,[133] SEC Commissioner Hester Peirce argued that, philosophically, it represented "a big step forward" toward expanding access to private markets.[134] She considered the change to signal additional non-

---

(comment by Co-Chair Hanks); *id.* at 53 ("[F]rankly the returns on capital are all in the private markets. Unaccredited investors only have public markets to actually invest in or they have real estate…") (comment by Mr. Nelson).

127 *See e.g., id.* at 28 ("[S]ome of the smartest investors I've ever seen know the company and the industry as opposed to the investing community.") (comment by Mr. Walsh); *id.* at 30–31 ("My uncle just died. He didn't go to college. He worked right out of high school… And when he died he had amassed a huge amount of investments. He would have never qualified under any of these rules… He knew the electrical industry, he knew it backward and forwards. He knew what would work in the short run and long run. He got his buddies together, they made an investment pool, and they invested in all these little technologies that, hey, maybe you're not going to see it grow, but he did quite well.") (comment by Ms. Yamanaka); *id.* at 44–45 ("I don't think we're talking about people who are going to take their first paycheck and put it into this. We're talking about I think a different level or segment of the population that has some sort of knowledge and they're not just investing in their 401K at their company level stock.") (comment by Ms. Yamanaka).

128 *2016 Report*, *supra* note 122, at 2.

129 *See 2016 Proceedings*, *supra* note 125, at 32.

130 *See* Amending the "Accredited Investor Definition", Securities Act Release No. 10734, at 22–27 (Dec. 18, 2019), https://www.sec.gov/rules/proposed/2019/33-10734.pdf [https://perma.cc/49TU-2MQY] [hereinafter *Proposing Release No. 10734*] (summarizing various recommendations to the SEC on expanding the accredited investor definition).

131 Accredited Investor Definition, Securities Act Release No. 10824, at 1 (Aug. 26, 2020), https://www.sec.gov/rules/final/2020/33-10824.pdf [https://perma.cc/B46M-L5TX] [hereinafter *Release No. 10824*] (final rule).

132 Lawrence J. Hass et al., *SEC Amends Definition of "Accredited Investor" and "Qualified Institutional Buyer"*, PAUL HASTINGS (Sept. 17, 2020), https://www.paulhastings.com/insights/client-alerts/sec-amends-definition-of-accredited-investor-and-qualified-institutional-buyer [https://perma.cc/U9ST-U4C9].

133 Hester Peirce & Chris Brummer, *Who Should Be An Accredited Investor?*, ROLL CALL: FINTECH BEAT at 23:15 (Sept. 15, 2020), https://www.rollcall.com/podcasts/fintech-beat/who-should-be-an-accredited-investor/ [https://perma.cc/EL8R-P6TU].

134 *Id.* at 23:50.

financial measures of sophistication, such as education, on the horizon.[135] Commissioner Peirce also expressed a personal belief that operational expertise might suffice for sophistication to participate in private markets. "Someone who has been a tractor repair person for her whole career," she noted, "might well be better able to assess whether or not a tractor manufacturer is going to succeed or fail with a new venture than someone who is really wealthy."[136]

Interestingly, the SEC subtly suggested the sophistication of intra-industry experts in a separate recent rulemaking. The Commission considered the potential effect of proposals for expanding non-accredited investors' access to exempt offering investment opportunities. It noted that the magnitude of such effect may depend on "whether issuers prefer accredited investors due to their industry connections and expertise."[137] This statement implies that industry connections and expertise, both of which intra-industry experts possess, could be highly persuasive factors for issuers deciding which investors they want involved in their offerings. Considered alongside actions of the Committee and Commissioner Peirce's remarks, the SEC appears to be gradually warming to the idea of enabling intra-industry experts' participation in the private markets.

2. Other Calls for Expanding Access to Intra-Industry Experts

Actors in the private sector and the legislature have similarly endorsed including intra-industry experts in the private markets. Although numerous relevant democratizing proposals have appeared over the decades,[138] the most comprehensive private sector proposal in recent years comes from Thaya Knight. Knight is the former associate director of financial regulation studies at the Cato Institute,[139] former counsel to Commissioner Peirce,[140] and current counsel to SEC Commissioner Elad Roisman.[141] In a 2016 set of policy recommendations made in response to the JOBS Act, Knight asserts that the accredited investor definition is underinclusive, needlessly excluding potential sophisticated investors from private

---

135 *See id.* at 25:25.

136 *Id.* at 27:55.

137 Facilitating Capital Formation, Securities Act Release No. 10884, at 195–96 (Nov. 2, 2020), https://www.sec.gov/rules/final/2020/33-10884.pdf [https://perma.cc/8RQB-B9VU] (final rule).

138 *See, e.g.*, Abraham J.B. Cable, *Mad Money: Rethinking Private Placements*, 71 WASH. & LEE L. REV. 2253, 2253 (2014) (proposing that all individuals be allowed to invest in private placements subject to an investment cap); C. Edward Fletcher, III, *Sophisticated Investors Under the Federal Securities Laws*, 1988 DUKE L.J. 1081, 1149–54 (1988) (identifying common qualities that courts have considered in determining investors' sophistication, including professional status, education, special access to information, and age, and arguing for their holistic consideration).

139 *Thaya Brook Knight*, CATO INST., https://www.cato.org/people/thaya-knight [https://perma.cc/AB7C-CKS7] (last accessed Nov. 23, 2021).

140 Thaya Knight, LINKEDIN, https://www.linkedin.com/in/thayaknight/ (last accessed Nov. 23, 2021).

141 *Id.*

offerings and depriving small businesses of capital raising opportunities.[142] She notes that the "best solution" to this problem is the outright elimination of the accredited/non-accredited investor dichotomy. She also suggests that the accredited investor definition should allow exempt offering participation upon a "showing that the investor has knowledge of the issuer's industry."[143] Specifically, she argues that "a certain amount of work experience in that industry, a professional qualification, or a university-level degree in a field directly related to the issuer's industry" should create a presumption of sophistication.[144] These suggestions have helped inform this Article.[145]

Other private sector calls for granting private markets access to intra-industry experts came via the comments solicitation period of recent SEC rulemaking. For example, the Biotechnology Innovation Organization recommended the SEC allow individuals with advanced educational degrees in the hard sciences (e.g., a relevant Doctor of Philosophy (PhD), Master of Science (MS), or Medical Doctor (MD)) to participate in exempt offerings.[146] The organization noted that such investors would have sufficient technical sophistication to adequately assess the business risks and opportunities of early-stage biotechnology companies, regardless of their financial sophistication.[147] David R. Burton echoed this sentiment. He argued that advanced scientific, engineering, medical, or technology degrees should qualify an investor to participate in private offerings of issuers relevant to their specific discipline.[148]

Beyond these private sector calls, legislators also supported the proposal. The Fair Investment Opportunities for Professional Experts Act, introduced in

---

142 Thaya Brook Knight, *A Walk Through the JOBS Act of 2012: Deregulation in the Wake of Financial Crisis*, 790 CATO INST. CTR. MONETARY & FIN. ALTERNATIVES POL'Y ANALYSIS 1, 16 (2016).

143 *Id. See also id.* at 30–31.

144 *Id.* at 16.

145 Knight further discusses intra-industry expertise in a separate publication by the Cato Institute. Addressing the proposal to allow securities industry experts to be accredited, she argues that the accredited investor standard should "be expanded to allow those with expertise in a particular field to invest in offerings related to that industry. Expertise could be defined as either a university-level degree in the field or a certain number of years of experience working in the industry." Thaya Brook Knight, *58. Securities Regulation*, *in* CATO HANDBOOK FOR POLICYMAKERS 588 (8th ed. 2017), https://www.cato.org/sites/cato.org/files/serials/files/cato-handbook-policymakers/2017/2/cato-handbook-for-policymakers-8th-edition-58_0.pdf [https://perma.cc/R65D-7LKT].

146 Letter from Carlo Passeri, Dir. of Capital Mkts. & Fin. Servs. Pol'y, Biotechnology Innovation Org., to Vanessa Countryman, Sec'y, Sec. & Exch. Comm'n 2 (June 16, 2020), https://www.sec.gov/comments/s7-25-19/s72519-7327897-218469.pdf [https://perma.cc/4PHV-TNGZ].

147 *Id.*

148 Letter from David R. Burton, Senior Fellow in Econ. Pol'y, Heritage Found., to Vanessa Countryman, Sec'y, Sec. & Exch. Comm'n 2 (May 1, 2020), https://www.sec.gov/comments/s7-25-19/s72519-7144449-216247.pdf [https://perma.cc/SH5J-DKJB].

separate forms in Congress by Representative David Schweikert in 2015[149] and 2017,[150] would have statutorily amended the accredited investor definition to encompass individuals with "demonstrable education or job experience [that would] qualify such person as having professional knowledge of a subject related to a particular investment, and whose education or job experience is verified by the Financial Industry Regulatory Authority or an equivalent self-regulatory organization."[151] This language was also included in Section 860 of the Financial CHOICE Act of 2017.[152] During debate over H.R. 2187, Rep. Schweikert explained the impetus for the bill by relaying a story of a town hall attendee. The attendee told Rep. Schweikert, "I have a Ph.D. in electrical engineering. I work at the Intel plant in Chandler. I have some friends that started a business a year or two ago [making computer components]. I am an expert … and I am not allowed to invest in it because I don't meet the income and assets threshold [of an accredited investor]."[153] In addition, on July 18, 2019, a group of thirteen U.S. Senators representing the Committee on Banking, Housing, and Urban Affairs sent a letter to the SEC in part recommending expanding the accredited investor definition to account for an individual's "qualifying education or expertise."[154]

B. Theoretical and Policy Justifications

1. Intra-Industry Experts Can Fend for Themselves

Opening the door to intra-industry experts' participation in the private markets aligns with the purpose and priorities of securities law. The Securities Act of 1933 and its registration requirements protect investors by ensuring that issuers provide the information necessary to make informed investment decisions.[155]

---

[149] H.R. 2187 (114th): Fair Investment Opportunities for Professional Experts Act, GOVTRACK, https://www.gov track.us/congress/bills/114/hr2187 [https://perma.cc/9JT4-BCFV] (last accessed Nov. 23, 2021).

[150] H.R. 1585 (115th): Fair Investment Opportunities for Professional Experts Act, GOVTRACK, https://www.govtrack.us/congress/bills/115/hr1585 [https://perma.cc/6BSS-HWF2] (last accessed Nov. 23, 2021).

[151] H.R. 1585, 115th Cong. (2017); H.R. 2187, 114th Cong. (2016).

[152] H.R. 10, 115th Cong. (2017).

[153] Brent J. Horton, *In Defense of a Federally Mandated Disclosure System: Observing Pre-Securities Act Prospectuses*, 54 AM. BUS. L.J. 743, 795 n. 273 (citing 162 Cong. Rec. H379 (2016) (statement of Rep. Schweikert)). A recording of Rep. Schweikert's statements is available online. *U.S. House of Representatives: House Session, Part 2*, C-SPAN (Feb. 1, 2016), https://www.c-span.org/video/?404021-101/us-house-legislative-business&event=404021&playEvent [https://perma.cc/3MZP-L3P2].

[154] Letter from Mike Crapo et al., Senator, U.S. Senate, to Jay Clayton, Chairman, Sec. & Exch. Comm'n (July 18, 2019), https://www.banking.senate.gov/download/letter-from-banking-committe e-republicans-to-sec [https://perma.cc/H4G8-GEUT].

[155] Ralston Purina Co., 346 U.S. at 124. *See also supra* Part II.A.

Throughout the statute's legislative history, Congressional Representatives have emphasized the need for transparency about issuers' underlying assets[156] and broader informational parity between issuers and investors.[157] Conversely, Congress seeks to provide registration exemptions for transactions where there is "there is no practical need for [the bill's] application,"[158] or where the participating investors can "fend for themselves"[159] and have sufficient access to information.[160] Pursuant to these aims, the SEC has repeatedly developed new transaction exemptions upon identifying instances in which offerees can fend for themselves.[161]

Intra-industry experts are capable of "fending for themselves" based on their advanced knowledge of industry operations and trends. This is true relative to ordinary retail investors. Additionally, this is true relative to existing accredited investors who, though presumed sophisticated based on their wealth or annual income,[162] might neither personally evaluate the merits of a specific investment for lack of expertise nor purchase investment advisory support.[163] Both empirical studies and general investment literature have documented that intra-industry experts are capable of translating their operational expertise into investment sophistication.

At least one study supports intra-industry experts' sophistication advantage. Daniel Bradley *et al.* conducted a study on the relative performance of professional investment analysts with prior work experience in the industry of their target investments.[164] The researchers found that analysts produce more accurate

---

156 77 Cong. Rec. 2914 (1933) ("The man who sells [securities] ought to give all the facts, and the Government ought to require the issuer of securities to give all the facts, and be honest with the public. This is the purpose of the legislation, so that every investor may know more about the assets behind the securities[.]") (statement of Rep. Greenwood).

157 77 Cong. Rec. 2918 (1933) ("The purpose of this bill is to place the owners of securities on a parity, so far as is possible, with the management of the corporations, and to place the buyer on the same plane so far as available information is concerned, with the seller.") (statement of Rep. Rayburn).

158 H.R. Rep. No. 85, 73d Cong., 1st Sess. at 5.

159 Ralston Purina, 346 U.S. at 125.

160 *Id.* at 125, 127.

161 *See supra* Part II.B-C.

162 *See Proposing Release No. 10734*, *supra* note 130, at 103 ("[G]iven the presumed financial sophistication of accredited investors, issuers may rely on Rule 506(b) and Rule 506(c) to offer securities on an unregistered basis to accredited investors without providing additional disclosure to those investors.").

163 Gregory Yadley, a member of the former SEC Advisory Committee on Small and Emerging Companies, explained that wealth and income are treated as a proxy for sophistication because wealthy investors are better suited to purchase investment advisory services, whether or not they practically choose to do so. Videoconferencing Interview with Gregory Yadley, Partner, Shumaker, Loop & Kendrick LLP (Feb. 16, 2021).

164 *See generally* Daniel Bradley et al., *Before an Analyst Becomes an Analyst: Does Industry Experience Matter?*, 72 J. FIN. 751 (2015).

forecasts and outperform peers when they have prior operational experience in the industry of firms they are forecasting.[165] The researchers' work further suggests that information asymmetry between investors and issuers is less pronounced for intra-industry experts relative to their nonexpert peers.[166] This study assessed individuals with substantial financial knowledge.[167] However, the findings seem to imply that industry expertise provides greater investment sophistication and additional relevant information on which to evaluate investments—collectively, the two hallmark characteristics for private market participation.[168]

Conventional investing wisdom reinforces the findings above. Peter Lynch, former Fidelity Investments mutual fund manager and investing guru, first popularized the concept that operational knowledge of an industry or issuer can enable better understanding of an investment's merits.[169] In his 1989 work *One Up on Wall Street*, Lynch wrote:

> "[I]f you sell tires, make tires, or distribute tires, you've got an edge in Goodyear. All along the supply lines of the manufacturing industry, people who make things and sell things encounter numerous stockpicking opportunities. It might be a service industry, the property-casualty insurance business, or even the book business where you can spot a turnaround… [In most] endeavors the grassroots observer can spot a turnaround six to twelve months ahead of the regular financial analysts. This gives an incredible head start in anticipating an improvement in earnings—and earnings, as you'll see, make stock prices go higher."[170]

Numerous commentators have since echoed this sentiment, with writers commonly touting the advantages of industry expertise in understanding an issuer's business fundamentals, position within the broader industry, and viability with

---

165 *Id.* at 751.

166 *See id.* at 776 ("Taken together, the results in this section suggest that a loss of analysts with related preanalyst industry experience has more pronounced effects on covered firms' level of information asymmetry and stock prices relative to loss of nonindustry expert analysts.").

167 Investment analysts, whether bolstered by industry expertise or not, are likely sophisticated purely by nature of their investment work. *See* Luis A. Aguilar, *Revisiting the "Accredited Investor" Definition to Better Protect Investors*, SEC. & EXCHANGE COMMISSION (Dec. 17, 2014), https://www.sec.gov/news/statement/spch121714laa.html [https://perma.cc/QBV8-U3SF].

168 *Supra* Part II.B.2.

169 Michael Sincere, *Stocks' Short-Term Signals Are Bullish But Peter Lynch's Long-Term Investing Advice Still Applies*, MARKETWATCH: OPINION (Apr. 9, 2021, 11:36 AM ET), https://www.marketwatch.com/story/stocks-short-term-signals-are-bullish-but-peter-lynchs-long-term-investing-advice-still-applies-11617920319 [https://perma.cc/QH4G-LWJM].

170 LYNCH, *supra* note 1, at 101.

respect to market trends.[171] Berkshire Hathaway CEO Warren Buffet summarized the concept with a maxim, "Never invest in a business you cannot understand."[172]

Given its corresponding advantages in evaluating investment opportunities, the SEC should consider intra-industry expertise a measure of sophistication. Sophisticated investors are those who "understand[] the risks of participating in unregistered offerings"[173] and "whose knowledge and experience render them capable of evaluating the merits and risks of a prospective investment—and therefore fending for themselves."[174]Although securities law has traditionally characterized the requisite investor sophistication for private offering participation in terms of financial and business knowledge and experience,[175] the actual parameters of sophistication have largely remained indeterminate.[176] Notably, several court opinions have implicitly recognized intra-industry expertise as a factor in measuring sophistication.[177] Accordingly, despite convention, the SEC is not precluded from adding intra-industry expertise as a measure of sophistication.[178]

---

171 *See, e.g.*, Catherine Brock, *How to Invest in What You Know*, MOTLEYFOOL (June 4, 2020), https://www.fool.com/investing/2020/06/04/how-to-invest-in-what-you-know.aspx [https://perma.cc/ECV3-8Y7C]; Joshua Kennon, *Invest in Stocks That You Know*, THEBALANCE (Jan. 28, 2020), https://www.thebalance.com/invest-in-what-you-know-356334 [https://perma.cc/ HYM3-GX5W].

172 Wayne Duggan, *Never Invest In Something You Don't Understand*, U.S. NEWS (May 11, 2017, 9:00 AM), https://money.usnews.com/investing/articles/2017-05-11/never-invest-in-something-you-dont-understand [https://perma.cc/2YLD-BESK].

173 Jay Clayton, *Statement on Modernization of the Accredited Investor Definition*, SEC. & EXCHANGE COMMISSION (Aug. 26, 2020), https://www.sec.gov/news/public-statement/clayton-accredited-investor-2020-08-26 [https://perma.cc/F9Q9-47QK].

174 *Release No. 10824*, *supra* note 131, at 26.

175 *See supra* Part II.B.2 (discussing the interpretation of Ralston Purina's sophistication standard). *See also Release No. 10824*, *supra* note 131, at 25–26 (emphasizing that an investor should have "a sufficient level financial sophistication to participate in investment opportunities that do not have the additional protections provided by registration under the Securities Act."); *Rule 506 of Regulation D*, SEC. & EXCH. COMM'N., https://www.investor.gov/introduction-investing/investing-basics/glossary/rule-506-regulation-d [https://perma.cc/KG7V-M8W9] (last accessed Nov. 23, 2021) (discussing sophistication within the context of non-accredited investors' participation in offerings under Rule 506 of Regulation D).

176 *Supra* Part II.B.2.

177 *See* Doran v. Petroleum Mgt. Corp., 545 F.2d 893, 902 (5th Cir. 1977) (noting that Doran's specialized education as a petroleum engineer, in part, evidenced his investment sophistication); SEC v. Asset Mgmt. Corp., No. IP 78-34-C., 1979 U.S. Dist. LEXIS 8080, at *28 (S.D. Ind. Dec. 10, 1979) ("The offerees did not meet the requisite sophistication test since only one offeree had any prior experience in the coal related industry.").

178 A 2015 report by the SEC considered a host of potential new criteria for determining sophistication, including education, professional certifications, and an accredited investor test, but limited its review to financial sophistication. SEC. & EXCH. COMM'N, REPORT ON THE REVIEW OF THE DEFINITION OF "ACCREDITED INVESTOR" 57–67 (2015), www.sec.gov/corpfin/reportspubs/special-studies/review-definition-of-accredited-investor-12-18-2015.pdf [https://perma.cc/VS6E-6QQZ]. An updated report which examined the impact on intra-industry expertise on investment

2. Intra-Industry Experts Would Facilitate Capital Formation and Promote Economic Performance in the Private Markets

As Congressionally mandated, the SEC maintains a three-prong mission: (1) protect investors, (2) maintain fair, orderly, and efficient markets, and (3) facilitate capital formation.[179] One mechanism for facilitating capital formation is expanding investor access to the capital markets. By expanding the pool of potential investors available to issuers exclusively interested in remaining private, which accounts for most firms,[180] the SEC would provide issuers with an increased source of capital to potentially access.[181] This rationale underlies recent efforts by the SEC to expand exempt offering channels.[182]

Furthermore, intra-industry experts could materially enhance the performance of the private markets in ways beyond their monetary investments. Private equity transactions are known for the knowledge-sharing relationship between issuers and investors, with issuers often pursuing investors with preexisting expertise in their industry.[183] By enabling issuers to access intra-industry expert investors who would otherwise be inaccessible for lack of wealth or income, the SEC would facilitate opportunities for investors to share their knowledge with private issuers. Such knowledge sharing could potentially be useful for small business private issuers who cannot otherwise afford expert advice.[184]

---

sophistication, both from a financial and business lens and an operational lens, would be prudent in understanding the costs and benefits of enacting this Article's proposal.

179 *About the SEC*, SEC. & EXCH. COMM'N (last accessed Nov. 23, 2021), https://www.sec.gov/about.shtml [https://perma.cc/G56K-VX86].

180 In a 2015 survey of 636 middle market companies, 92% of respondents indicated that they had no plans for publicly listing on a stock exchange. BRIAN KNIGHT, MILKEN INST., ACCESS TO CAPITAL: HOW SMALL AND MID-SIZE BUSINESSES ARE FUNDING THEIR FUTURE 27 (2016), https://www.sec.gov/info/smallbus/acsec-022516-access-to-capital-brian-knight.pdf [https://perma.cc/6BF6-TY33].

181 Videoconferencing Interview with David Lynn, Partner, Morrison & Foerster LLP (Feb. 10, 2020).

182 *See, e.g.*, SCOTT W. BAUGUESS, SEC. & EXCH. COMM'N, PRIVATE SECURITIES OFFERINGS POST-JOBS ACT 10 (2016), https://www.sec.gov/info/smallbus/acsec/private-securities-offerings-post-jobs-act-bauguess-022516.pdf [https://perma.cc/FP74-QC52] (noting that general solicitation under 506(c) could facilitate capital formation by lowering the search cost of issuers finding accredited investors and provide investors with more investment opportunities).

183 Private equity investors have also been known to specifically pursue private investment opportunities in the industries that they know best. *See* Andrew Sherman, Statement at the 28th Annual Securities and Exchange Commission Government-Business Forum on Small Business Capital Formation, in Record of Proceedings 37 (Nov. 19, 2009), https://www.sec.gov/info/smallbus/sbforumtrans-111909.pdf [https://perma.cc/P8AW-CTYG] (identifying a trend of increasing venture capital investments in "companies that are [] in your expertise wheel house").

184 *2016 Proceedings*, *supra* note 125, at 33 ("[Industry expert private investors] provide more than their money, they provide their knowledge, their expertise, their, you know, their connections… [In this hypothetical private investor group,] we don't have neurosurgeons in our groups, but we have doctors and doctors who know neurosurgeons. And the next thing you know, before you know it,

Policy debates regarding the capital markets often position capital formation in opposition to investor protection.[185] As such, a common critique holds that expanding investors' access to exempt offerings will invariably increase the incidence of securities fraud.[186] Though theoretically valid, especially as fraud prevention is a cornerstone goal of the SEC,[187] this critique lacks concrete support. First, there is scant evidence to suggest that expanding access to the private markets produces a corresponding uptick in fraud.[188] Second, public discourse at times conflates protection from fraud with protection from loss,[189] and critics should note that the Securities Act was not intended to prevent loss on account of knowledgeable but poor investment decisions.[190] Venturing into the latter conception of securities law raises the specter of paternalism, a criticism which has

---

we're calling the head of neurosurgery at Columbia University because one of our doctors knew him, went to med school with him. So that got us someone who could help advise on making those decisions.") (comment by Ms. Mott).

185 EVA SU, CONG. RES. SERV., INTRODUCTION TO FINANCIAL SERVICES: CAPITAL MARKETS 2 (2021), https://crsreports.congress.gov/product/pdf/IF/IF11062 [https://perma.cc/9HCG-B38G].

186 *See, e.g.*, Pollman, *supra* note 24, at 356 ("[T]he relative dearth of enforcement in the private market, which is surging in size and opaque with respect to the pervasiveness of securities fraud, gives rise to serious concerns about efficient capital allocation[.]"); Daniel J. Morrissey, *The Securities Act at its Diamond Jubilee: Renewing the Case for a Robust Registration Requirement*, 11 U. PA. J. BUS. L. 749, 754, 772, 785 (excoriating Regulation D's enablement of wealthy individuals' participation in the private markets for diminishing investor protections and facilitating elder fraud).

187 Westbrook & Westbrook, *supra* note 115, at 704, 705; C. Steven Bradford, *Crowdfunding and the Federal Securities Law*, 2012 COLUM. BUS. L. REV. 1, 98 (2012), https://digitalcommons.unl.edu/cgi/viewcontent.cgi?article=1118&context=lawfacpub [https://perma.cc/FW2N-MKY9].

188 *See, e.g.*, RACHITA GULLAPALLI, SEC. & EXCH. COMM'N, MISCONDUCT AND FRAUD IN UNREGISTERED OFFERINGS: AN EMPIRICAL ANALYSIS OF SELECT SEC ENFORCEMENT ACTIONS 1 (2020), https://www.sec.gov/files/Misconduct%20And%20Fraud%20In%20Unregistered%20Offerings.pdf [https://perma.cc/AJL6-VAF3] (finding only 210 unique SEC enforcement actions out of more than 73,000 exempt offerings conducted during a two-year period); *Proposing Release No. 10734*, *supra* note 130, at 102 ("we are not aware from our enforcement experience or otherwise of disproportionate fraud" due to the expansion of the accredited investor pool with inflation); BAUGUESS, *supra* note 182, at 11 (noting that there was "no measured increase in the incidence of fraud in [the] new Rule 506(c) market").

189 *See 2016 Proceedings*, *supra* note 125, at 36 (comment by Gregory Yadley).

190 *See id.* at 41 ("[I]t seems a little bit out of bounds when we start trying to protect people from themselves as opposed to trying to protect people from fraudsters") (comment by Co-Chair Graham). Case law interpreting the Securities Act has historically rebuffed the notion of ability to absorb loss as a basis for investor participation in exempt offerings. Cable, *supra* note 138, at 2315. *But see* Securities Act Release No. 9974, at 26 (Oct. 30, 2015), https://www.sec.gov/rules/final/2015/33-9974.pdf [https://perma.cc/WFU7-MQDX] (explaining that investment limits tiered by income and net worth are designed to "potentially limit investment losses" by "investors who may be less able to bear the risk of loss."). Loss prevention has also not justified the creation of investor protections such as investment limits in the public markets. Jennifer J. Schulp, *Let Investors Decide, Part 1*, CATO INST.: CATO AT LIBERTY (June 1, 2020, 8:33 AM), https://www.cato.org/blog/let-investors-decide-part-1 [https://perma.cc/LW86-RDAJ].

long dogged the SEC with respect to its restrictive treatment of the private markets.[191]

Finally, expanding access to exempt offerings will not diminish investor protections, if done responsibly. Intra-industry experts are arguably better equipped to deal with fraudsters, due to their technical knowledge, as opposed to investors accredited because of their wealth. Wealth and income are considered a proxy for access to financial sophistication.[192] However, wealthy investors can be easily defrauded if they choose not to employ sophisticated advisors for assistance, whereas intra-industry experts have personal knowledge on which to rely for investment evaluations. Although the risk of loss is inherent in private market investments,[193] financial harm is also inherent in limiting sophisticated investors to the public markets.[194] This is a cost of stringent investor protections that the SEC must consider.[195] If sound conditions are in place to ensure that "intra-industry expert" necessarily means only sophisticated investors, this Article's proposal could simultaneously expand capital formation opportunities, mitigate income inequality, and maintain sufficient investor protection.

---

[191] *See, e.g.*, Schulp, *supra* note 190 ("The SEC decides who gets to invest where: public markets only for most, but public and private markets for the wealthy. Such paternalism is objectionable in itself."); Letter from James J. Angel, Assoc. Professor of Fin., Georgetown Univ., to Sec. & Exch. Comm'n (Mar. 3, 2020), https://www.sec.gov/comments/s7-25-19/s72519-6898005-211087.pdf [https://perma.cc/6FQY-5LKN] (characterizing the restrictive nature of access to private markets as producing a "caste system of investing that perpetuates inequality"); Berlau, *supra* note 106 (calling the restrictive accredited investor system an "outdated paternalistic intervention into the economic freedom of Americans.").

[192] Videoconferencing Interview with Gregory Yadley, Partner, Shumaker, Loop & Kendrick LLP (Feb. 16, 2021).

[193] *See* Bradford, *supra* note 187, at 99; *Investor Bulletin: Private Placements Under Regulation D*, SEC. & EXCH. COMM'N (Sept. 24, 2014), https://www.sec.gov/oiea/investor-alerts-bulletins/ib_privateplacements.html [https://perma.cc/98EN-RSF5] ("Private placements may offer great opportunity. However, the attractive potential rewards often come with high risks of loss.").

[194] *See supra* Part II.C.2. *See also* MILLSTEIN CTR. & COLUM. L. SCH., PRIVATE OWNERSHIP AT A PUBLIC CROSSROADS: STUDYING THE RAPIDLY EVOLVING WORLD OF CORPORATE OWNERSHIP 10 (2019), https://millstein.law.columbia.edu/sites/default/files/content/docs/Private%20Ownership%20at%20a%20Public%20Crossroads%20White%20Paper%20(Final)%20(2.11.19).pdf [https://perma.cc/KVD5-7KYV] (characterizing the reduced ability to diversify portfolios in the public markets as a harm for ordinary investors).

[195] Arthur Levitt, Chairman, Sec. & Exch. Comm'n, Speech to the Commonwealth Club of San Francisco, California (May 17, 1996), https://www.sec.gov/news/speech/speecharchive/1996/spch101.txt [https://perma.cc/T7GV-N2S2] (for any rule governing market behavior, "the SEC is called upon to decide whether the investor protection afforded by the rule is worth the cost imposed.").

IV. MECHANICS OF THE PROPOSAL

A. Defining Intra-Industry Expertise

1. "Intra-Industry"

To establish sophistication, investors in this proposal must operate in the same industry as the issuer in whose offering they wish to invest. Industry classification can be a difficult task, with many companies operating in either new business sectors or in multiple industries contemporaneously, thereby defying clear-cut categorization into a single industry.[196] Given the unique specialization needed to manage these challenges effectively, determining the issuer's and investor's industries should depend on an industry classification system developed outside of the SEC.[197]

There are two major government-sourced classification systems and three major private sector-sourced classification systems. The government-sourced classification systems are the Standard Industrial Classification (SIC) system and the North American Industry Classification System (NAICS). The U.S. government created the SIC in 1937 to facilitate the collection and sharing of industry data across agencies.[198] They released the NAICS in 1997 with Mexico's Instituto Nacional de Estadistica y Geografia, Statistics Canada, and the U.S. Economic Classification Policy Committee.[199] Major private sector efforts in industry classification include the Global Industry Classification Standard, published by Standard & Poor's and Morgan Stanley Capital International in 1999; the Industry Classification Benchmark, launched in 2005 by Dow Jones & Co. and the Financial Times Stock Exchange; and the 2004 Thomson Reuters Business Classification.[200]

The SIC is likely the best choice of an established industry classification for use in this proposal. The SEC's EDGAR database currently utilizes SIC Codes to organize public corporate disclosures, and the SEC Division of Corporation Finance uses SIC as a basis for assigning staff review responsibility for companies'

---

196 *See* Michael Kozlov et. al, *Modern Challenges in Industry Classification*, WORLDQUANT (Mar. 31, 2020), https://www.weareworldquant.com/en/thought-leadership/modern-challenges-in-company-classification/ [https://perma.cc/M7YS-U37H].

197 Videoconferencing Interview with David Lynn, Partner, Morrison & Foerster LLP (Feb. 10, 2020).

198 Kozlov et al., *supra* note 196.

199 *North American Industry Classification System – NAICS*, U.S. CENSUS BUREAU, https://www.census.gov/naics/ [https://perma.cc/RU53-UMAL] (last accessed Nov. 23, 2021).

200 Kozlov et al., *supra* note 196.

filings.[201] In doing so, the SEC does not actively assign industry codes to companies; instead, they rely on the predetermined SIC designation.[202] Companies traditionally have an opportunity to change their designation. For example, if they feel that the nature of their business has fundamentally changed, it is subject to review by the SEC.[203]

Consequently, I recommend the SEC use SIC to determine the industry of issuers conducting exempt offerings when extending accredited investor status to intra-industry experts. The principles and procedures that the SEC established to use SIC in other contexts can directly apply to this proposal's implementation, mitigating concerns about administrative burden. Issuers can also rely on SIC to determine if their offerees work within their industry, potentially qualifying issuers as intra-industry. This practice is likely familiar and comfortable for issuers, as businesses commonly use SIC Codes "to determine what industries customers operate in" for purposes of marketing, sales, market segmentation, and more.[204]

2. "Expertise"

Expertise forms the second key condition of this investor class. To qualify for accredited investor status under this proposal, the investor must have sufficient operational or technical expertise in the industry of the issuer. Problems arise when determining both the appropriate measures of "expertise" (e.g., education) and the attributes or level needed within those measures to constitute "expertise" (e.g., obtaining a Bachelor of Science (B.S.) versus a Master of Science (M.S.) in a given discipline). I propose that the SEC allow investors to establish their expertise by any of the following measures: professional certifications, education, and work experience.[205]

The SEC's recent accredited investor definitional amendments explicitly granted accredited investor status to individuals who passed certain professional examinations and hold their corresponding certifications in good standing.[206] Professional certifications and licenses are the most logical extension of these amendments. The SEC emphasized that professional certifications and other credentials "provide a reliable indication that an investor has a sufficient level of

---

201 *Division of Corporation Finance: Standard Industrial Classification (SIC) Code List*, SEC. & EXCH. COMM'N, https://www.sec.gov/info/edgar/siccodes.htm [https://perma.cc/YFT7-CHE6] (last modified June 7, 2021).

202 Broc Romanek, *SIC Codes: How Does the SEC Assign Them?,* THECORPORATECOUNSEL.NET (Mar. 9, 2016), https://www.thecorporatecounsel.net/blog/2016/03/sic-codes-how-does-the-sec-assign-them.html [https://perma.cc/4FHB-ZURP].

203 *Id.*

204 *What is a SIC Code?*, SICCODE, https://siccode.com/page/what-is-a-sic-code# [https://perma.cc/6LGX-8G8M] (last accessed Nov. 23, 2021).

205 These measures directly echo the proposal of Thaya Knight. Knight, *supra* note 142, at 16.

206 *Release No. 10824*, *supra* note 131, at 29.

financial sophistication" to participate in exempt offerings.[207] This grant extended only to Series 7, Series 65, and Series 82 licenses but was intended as "a measured approach," which provided the Commission with "flexibility" to designate other qualifying certifications, designations, or credentials in the future.[208] Although limited to the disciplines of securities and investing, this provision provides a readymade framework, including a non-exclusive list of attributes expected of qualifying certifications enumerated in Rule 501(a)(10) and an accredited investor verification process,[209] for application to experts outside the securities and investing industries. Reputable non-financial professional licenses abound, such as the Professional Engineer's License[210]or the Certified Information Systems Security Professional certification,[211] providing an accessible, established avenue for individuals across industries to demonstrate their expertise.

Education is an appropriate measure of expertise because of its historical association with sophistication.[212] Knight suggested that "a university-level degree in a relevant field" would be sufficient to demonstrate expertise.[213] However, the Commission's objective of investor protection may warrant a stricter initial threshold. Deferring to the proposals by the Biotechnology Innovation Organization[214] and the Heritage Foundation,[215] I suggest a graduate-level degree, such as an M.S., Ph.D., or M.D., in the relevant issuer's field as an appropriate minimum level of education to qualify as an expert. This provides flexibility to test the efficacy of the broader proposal; if shown to be effective at protecting investors, it can expand to encompass certain four-year college degrees and trade school degrees.

Similarly, professional experience can reflect expertise based upon the ways in which it supports informed investment decisions in the relevant field[216] and its historical association with sophistication.[217] The main challenge with using professional experience to demonstrate expertise resides in the inconsistent

---

207 *Id.* at 25–26.

208 *Id.* at 32.

209 *See id.* at 29–33 (detailing elements of the qualifying framework, including issuers' responsibility to verify investors' accredited status and rejecting individuals' self-certification of sophistication).

210 *Professional Engineering Licensure*, AM. INST. CHEM. ENG'RS, https://www.aiche.org/careers/professional-engineering-licensure [https://perma.cc/QH24-3736] (last accessed Nov. 23, 2021).

211 *CISSP – The World's Premier Cybersecurity Certification*, (ISC)², https://www.isc2.org/Certifications/CISSP# [https://perma.cc/SJA3-YM82] (last accessed Nov. 23, 2021).

212 Fletcher, *supra* note 138, at 1151.

213 Knight, *supra* note 142, at 16.

214 Passeri, *supra* note 146, at 2.

215 Burton, *supra* note 148, at 2 (recommending accredited investor status for those with "advanced degrees").

216 *Supra* Part III.B.1.

217 Fletcher, *supra* note 138, at 1149–50.

measurement techniques and indicators.[218] Despite what Malcolm Gladwell may lead you to believe,[219] knowing the specifics required of each field is quite difficult. Becoming an expert in one field may require a different depth of experience and duration of practice than some other field.[220] For example, five years as a software developer at Apple may sufficiently qualify an individual as an expert in consumer software companies, but five years in the construction of office buildings may not qualify one as an expert in real estate companies. The former experience provides a holistic understanding of the software design process, user experience, and consumer interest and expectations. In contrast, the latter experience does not generally communicate fundamental business knowledge relevant to investment decision-making. The SEC expressed similar caution in expanding the accredited investor definition, rejecting requirements that investors actively practice in the fields related to the qualifying certifications or have practiced for a minimum number of years.[221] It noted that such criteria would be too complex for investors seeking to demonstrate sophistication and issuers seeking to verify accredited investor status.[222]

B. Potential Measures to Bolster Investor Protection

Despite the limited evidence of increased investor fraud following democratizing developments in the private markets,[223] investor protection remains an evergreen, valid objective for the SEC. Accordingly, the Commission may consider instituting additional protectionary requirements for intra-industry experts seeking to participate in exempt offerings. This Part outlines several potential options.

1. Prior Investment Experience or Financial Knowledge

The Commission could minimize concerns about exploitation of intra-industry experts in private market transactions by conditioning accredited investor status upon meeting a specified threshold of prior investment experience or demonstrated financial knowledge. This suggestion does not inherently undermine

---

218 K. Anders Ericsson et al., *The Making of an Expert*, HARV. BUS. REV. (July 2007), https://hbr.org/2007/07/the-making-of-an-expert [https://perma.cc/6BZX-HA99].

219 Malcolm Gladwell popularized the "ten-thousand-hour rule," which suggests that one can master a skill after ten thousand hours of practice; though even he admits that it is "a mistake to assume that the ten-thousand-hour idea applies to every domain." Malcolm Gladwell, *Complexity and the Ten-Thousand-Hour Rule*, NEW YORKER (Aug. 21, 2013), https://www.newyorker.com/sports/sporting-scene/complexity-and-the-ten-thousand-hour-rule [https://perma.cc/MC4X-YY8Z].

220 *See* Ericsson et al., *supra* note 218.

221 *Release No. 10824*, *supra* note 131, at 28.

222 *Id.*

223 *See supra* Part III.B.2.

the conceptual validity of intra-industry expertise; rather, it directly aligns this Article's proposal with the Commission's commonly articulated conception of sophistication (i.e., that "sophistication" implicitly means "financial sophistication").[224] In fact, the SEC Advisory Committee on Small and Emerging Companies posed this idea during their 2016 meeting. Some Committee members suggested that previous experience in investing in exempt offerings might provide investors with "the tools to understand what they need to look for in future investments."[225] Others noted that this requirement could be logically inconsistent[226] or of limited practical value.[227]

Prior investment experience could be an appropriate mechanism for investor protection, but it must comport with the private markets landscape. For example, the requirement could stipulate that an intra-industry expert participating in a Rule 506(c) or Rule 506(b) offering as an accredited investor must have previously participated as a non-accredited but sophisticated investor in a prior Rule 506(b) offering. Requiring prior private placement experience sounds great: participating in a private placement as a non-accredited investor would provide important insights for the new accredited investor's subsequent Regulation D investment. But it fails to acknowledge that most Regulation D offerings exclude non-accredited investors entirely,[228] limiting its feasibility.

A more suitable rule could require that intra-industry experts must have previously participated in other instance(s) of exempt offerings, such as offerings conducted pursuant to Regulation A or Regulation Crowdfunding. To measure investment experience more generally, the rule could require that investors have previously participated in a certain number of investments, whether public or private.[229] Alternatively, the rule could require intra-industry experts to demonstrate financial knowledge through a standardized accredited investor financial exam.[230] The SEC has acknowledged the potential for such an exam but has yet to adopt it.[231]

---

224 *See supra* Part III.B.1.

225 *2016 Proceedings*, *supra* note 125, at 19–20 (comment by Mr. Gomez).

226 *Id.* at 19 ("I don't see how you get the experience—if you can't qualify [for the prior exempt offering] you can't get the experience [needed for the subsequent exempt offering].") (comment by Ms. Mott).

227 *Id.* at 20 ("I'm not sure if I understand, Sebastian … because you're saying that if you qualified before but then you lost all your money because you did such a bad job investing and you no longer qualify, as long as there were ten bad investments you [could qualify again based on prior investment experience].") (comment by Co-Chair Graham).

228 BAUGUESS ET AL., *supra* note 98, at 35 (only 7% of Rule 506(b) offerings from 2009–2017 included or intended to include nonaccredited investors).

229 *See 2016 Proceedings*, *supra* note 125, at 15–17 (comments by Co-Chair Graham).

230 *Id.* at 18 (comment by Co-Chair Graham).

231 *Release No. 10824*, *supra* note 131, at 32.

2. Individual Investment Limits

The SEC could reinforce investor protection for intra-industry experts by imposing individual investment limits on them.[232] This may cut against the potential democratizing effect of my proposal by limiting intra-industry experts' participation in the private markets. However, it would likely mitigate the potentially significant loss from bad investments. Abraham Cable previously presented this limitation as the cornerstone feature of an academic proposal that would open the door for all retail investors to participate in the private markets.[233]

This type of protective rule could mirror the investment limits placed on non-accredited investors participating in Regulation Crowdfunding and Regulation A Tier 2 exempt offerings.[234] During the Committee debate, Gregory Yadley suggested that the investment limit rules of Regulation Crowdfunding serve as the basis for any investment limits applied to the current proposal because of their relative simplicity.[235] However, he noted a personal reluctance to endorse investment limitations,[236] a sentiment shared by others on the committee.[237]

3. Supplemental Access of Issuer Information

Finally, the SEC may consider implementing a suggestion from this Article's proposal, that would require issuers to furnish supplemental information regarding their underlying business to intra-industry expert offerees. This protective measure has its conceptual roots in *Doran v. Petroleum Management Corp.*,[238] in which the Court held that an offering did not meet the standards of a private placement due to insufficient provision of information to offerees.[239] Although the Court noted that Doran was sophisticated partly because of his expertise as a petroleum engineer,[240] it found that "sophistication is not a substitute

---

232 *2016 Proceedings*, *supra* note 125, at 44 ("I don't know what the answer is but, you know … I could see room for [investment] limits. I don't know what they might be, but I can some sort of limitation.") (comment by Co-Chair Graham).

233 *See generally* Cable, *supra* note 138.

234 *Overview of Capital-Raising Exemptions**, U.S. SEC. & EXCH. COMM'N, https://www.sec.gov/smallbusiness/exemptofferings/exemptofferingschart [https://perma.cc/SQP3-P9HY] (last modified Mar. 29, 2021).

235 *2016 Proceedings*, *supra* note 125, at 45.

236 *Id.* at 46.

237 *See id.* at 42–43 (comments by Ms. Yamanaka); *id.* at 47–48 ("I think you have to be really careful with limitations because you're going to shoot yourself in the foot … [T]hese people are not going to get the opportunity to invest [because of issuers' reluctance to bring in many small investors].") (comment by Ms. Tierney).

238 545 F.2d 893 (5th Cir. 1977).

239 *Id.* at 897.

240 *Id.* at 902.

for access to the information" that an investor would possess in a public offering.[241] The Court summarized its rationale:

> In short, there must be sufficient basis of accurate information upon which the sophisticated investor may exercise his skills. Just as a scientist cannot be without his specimens, so the shrewdest investor's acuity will be blunted without specifications about the issuer. For an investor to be invested with exemptive status he must have the required data for judgment.[242]

Intra-industry experts can only make informed investment decisions when they have adequate issuer-specific information to which to apply their operational or technical expertise. In most cases, issuers conducting a private placement will provide private placement memoranda (PPM) to offerees.[243] PPM are voluntary undertakings that are not typically reviewed by any regulator, but they tend to provide useful information about the issuer.[244] One survey found that every private offering involved some degree of disclosure, with some PPM tantamount to the prospectus provided in a registered offering.[245] Additionally, the information contained within the PPM is subject to the anti-fraud provisions of federal securities law.[246]

Even so, the SEC may promote additional information provisions to intra-industry experts by requiring private placements to feature a disclosure system like Regulation Crowdfunding.[247] This would bring private placement disclosures within an established regulatory mechanism. However, it would potentially undermine the "real benefit" of Regulation D's flexible disclosure policies[248] and disincentivize the use of the private placement exemption more generally.[249]

---

241 *Id.*

242 *Id.* at 903.

243 *Investor Bulletin: Private Placements Under Regulation D*, U.S. SEC. & EXCH. COMM'N (Sept. 24, 2014), https://www.sec.gov/oiea/investor-alerts-bulletins/ib_privateplacements.html [https://perma.cc/5KCR-GRE2].

244 *Id.*

245 Andrew N. Vollmer, *Abandon the Concept of Accredited Investors in Private Securities Offerings*, 49 SEC. REG. L.J. 5, 13 (2021).

246 Mark Astarita, *Introduction to Private Placements – A Securities Lawyer Guide*, SEC L., https://www.seclaw.com/introduction-private-placements/ [https://perma.cc/S3ZP-GN6S] (last accessed Nov. 23, 2021).

247 *Regulation Crowdfunding: A Small Entity Compliance Guide for Issuers*, U.S. SEC. & EXCH. COMM'N (Apr. 5, 2017), https://www.sec.gov/info/smallbus/secg/rccomplianceguide-051316.htm [https://perma.cc/M3Q8-KZQW].

248 Vollmer, *supra* note 245, at 16.

249 Regulation A provides an illustration of how increased disclosure mandates can depress issuers' reliance on an exemption. The relatively rigorous and costly public filing and disclosure requirements imposed by Regulation A, consequently referred to as a "mini-IPO," resulted in Regulation A being substantially underutilized by issuers. Gary J. Kocher et al., *The SEC Delivers*

V. CONCLUSION

Some commentators suggest that securities law has a "dirty little secret," privileging wealthy investors with exclusive access to private investment opportunities.[250] This phenomenon, in which a limited class of wealthy investors can access attractive exempt offerings, potentially exacerbates economic, social, and political inequalities in the U.S.[251] SEC Commissioner Elad Roisman described it as "fundamentally unfair, unequal, and unjustified."[252]

The SEC took a commendable first step toward democratizing access to the private markets in its recent expansion of the accredited investor definition. It acknowledged that wealth should not be the sole means to determine sophistication[253] and identified an initial opportunity to responsibly promote greater capital formation, all the while emphasizing caution and the need to safeguard vulnerable investors.[254] The SEC should continue this democratizing effort by recognizing another class of investors who can fend for themselves—intra-industry experts. These experts can effectively utilize their superior operational or technical knowledge to evaluate investment opportunities within their industry specialization.[255] Their industry-specific sophistication deserves recognition by way of accredited investor status. Enabling their private market participation would promote economic fairness, facilitate capital formation, and benefit small-business issuers in need of expert advice.

Although similar proposals have appeared in other realms of intellectual discourse, this Article represents the first attempt that the author has found to present the argument in a work of academic scholarship.[256] I convey the policy and practical justifications for the proposal,[257] offer a possible model for implementing

---

A+ Effort: New Rules Designed to Breathe Life into Regulation A, K&L GATES (Apr. 23, 2015), https://www.klgates.com/The-SEC-Delivers-A-Effort-New-Rules-Designed-to-Breathe-Life-into-Regulation-A-04-23-2015 [https://perma.cc/CN5G-WQAD].

250 Usha Rodrigues, *Securities Law's Dirty Little Secret,* 81 FORDHAM L. REV. 3389, 3389 (2013), https://digitalcommons.law.uga.edu/cgi/viewcontent.cgi?article=1938&context=fac_artchop [https://perma.cc/MF56-EAHH].

251 *See id.*; *supra* Part II.B.2.

252 Elad L. Roisman, *Commissioner Roisman Statement on Amending the "Accredited Investor" Definition*, U.S. SEC. & EXCH. COMM'N (Aug. 26, 2020), https://www.sec.gov/news/public-statement/roisman-statement-amendments-accredited-investor-definition [https://perma.cc/UZ6T-HPZD].

253 Clayton, *supra* note 173.

254 *See supra* Part III.A.1.

255 *Supra* Part III.B.1.

256 In researching this Article, I asked multiple professors and seasoned practitioners in securities law if they were aware of any academic scholarship concerning calls for private market participation by intra-industry expert. All responded in the negative.

257 *Supra* Part III.

the proposal,[258] and respond to counterarguments.[259] I believe that this proposal offers a valuable opportunity to responsibly democratize the private capital markets, and it is timely. At the time of publication, numerous developments are underway to address the same objective. For example, in September 2021, the SEC's Asset Management Advisory Committee unanimously approved a recommendation to increase retail investors' access to private equity vehicles.[260] Additionally, in October 2021, the founders of Forge Global Inc. announced plans to launch a publicly listed closed-end exchange-traded fund to let retail investors bet on early-stage growth companies.[261]

During my research, I encountered challenges due to the lack of relevant academic scholarship and empirical research. Although some scholars have produced excellent work on closely related themes,[262] none have directly addressed the sophistication of intra-industry experts. Empirical research is similarly lacking; future studies should empirically measure the investment advantage of intra-industry expertise and estimate how many individual investors would gain access to the private markets via this Article's proposal.[263] I hope this Article will spur additional study in these areas.

---

258 *Supra* Part IV.

259 *See supra* Part III.B.2 (responding to concerns that expanding private market access increases the likelihood of securities fraud); *supra* Part IV.B (outlining supplemental measures that would bolster investor protections in expanding the accredited investor definition to cover intra-industry experts).

260 Chris Cumming, *SEC Panel Backs Letting Ordinary Investors into Private Equity*, WALL ST. J. (Sept. 27, 2021, 5:42 pm ET), https://www.wsj.com/articles/sec-panel-backs-letting-ordinary-investors-into-private-equity-11632778962 [https://perma.cc/D4A6-FYJ5].

261 Justin Bear, *Fund to Let Retail Investors Bet on Early Tech Startups*, WALL ST. J. (Oct. 14, 2021, 9:45 am ET), https://www.wsj.com/articles/fund-to-let-retail-investors-bet-on-early-tech-startups-11634216400 [https://perma.cc/936E-LH44].

262 *See, e.g.*, Vollmer, *supra* note 245 (advocating for an elimination of the accredited investor distinction in favor of a universal disclosure system); Pollman, *supra* note 24 (discussing potential fraud corresponding with greater investor access to private offerings); Cable, *supra* note 138 (proposing investment limits as a means to facilitate universal participation in the private markets).

263 Notably, in its recent expansion of the accredited investor definition, the SEC was similarly hampered by data limitations in estimating how many investors would newly qualify as accredited investors. *Release No. 10824*, *supra* note 131, at 100, 102.