



February 25, 2025

The Honorable Ann Wagner
Chairwoman
Capital Markets Subcommittee
U.S. House of Representatives
Washington, DC 20515

The Honorable Brad Sherman
Ranking Member
Capital Markets Subcommittee
U.S. House of Representatives
Washington, DC 20515

Re: Capital Markets Subcommittee Hearing Entitled “The Future of American Capital: Strengthening Public and Private Markets by Increasing Investor Access and Facilitating Capital Formation”

Dear Chairwoman Wagner and Ranking Member Sherman:

The Small Business Investor Alliance (SBIA) submits this letter for the scheduled February 26th hearing of the Capital Markets Subcommittee to examine reforms that will further strengthen the U.S. capital markets, facilitate capital formation for small businesses, and create more opportunities to invest in both the public and private markets. SBIA appreciates the Subcommittee prioritizing capital formation issues during the 119th Congress.

SBIA is a national association that develops, supports, and advocates on behalf of policies that benefit investment funds that finance small and mid-size businesses in the lower middle market, as well as the investors that provide capital to these funds. Our membership consists of the advisers of traditional 3(c)(1) and 3(c)(7) private funds, small business investment companies (“SBICs”), rural business investment companies (“RBICs”), funds registered as business development companies (“BDCs”) under the Investment Company Act of 1940, and the investors that invest in these funds including banks, family offices, and fund of funds.

While SBIA is supportive of several bills the Subcommittee will examine during the hearing, we wish to provide our views and strong support for the following bills in particular:

H.R. ___ to exempt business developments companies (BDCs) from the acquired fund fees and expenses (AFFE) rule

This bill would correct a regulatory mandate that has resulted in investors receiving fundamentally misleading and inaccurate information about the costs of BDC investment.

When the SEC adopted the acquired fund fees and expenses (AFFE) rule in 2006, it did not adequately consider the unique structure of BDCs and how AFFE would affect BDCs and their portfolio companies. AFFE is intended to provide investors with a picture of total costs when a mutual fund they are invested in invests in other funds. However, when applied to BDCs, AFFE provides a misleading picture of the true cost of investing in BDCs – effectively “double counting” the expenses of a BDC investment. Investors are left ill-informed about the costs of an investment which negatively affects their ability to make sound decisions about their portfolio.

BDCs are an indispensable source of capital for thousands of smaller businesses in the United States. BDCs are required by law to invest 70% of their assets in “eligible portfolio companies” which are generally defined as U.S.-based businesses with a value of \$250 million or less. BDCs are also required by law to provide managerial assistance to their portfolio companies in order to help these businesses grow and prosper. Today there are roughly 139 BDCs with over \$300 billion invested in businesses across the country.

Because of the treatment of BDCs under AFFE, certain index providers began dropping BDCs from indices, which in turn led to an outflow of institutional investor dollars in BDCs. This translates to a reduction in capital that BDCs can deploy to middle market and lower middle market businesses throughout the country. Exempting BDCs from the AFFE rule is necessary to incentive institutional investment back into BDCs.

SBIA has appreciated the chance to work with both members of the aisle on this critical issue and are hopeful that Congress can work on a bipartisan basis to enact an AFFE fix in the coming months.

H.R. the Small Business Investor Capital Access Act

SBIA commends Rep. Barr for again introducing this legislation, which would adjust for inflation the assets under management (AUM) threshold that triggers SEC registration for private funds.

In 2010, Congress replaced the longstanding private fund exemption from SEC registration requirements with a set of narrower exemption criteria. Amongst these criteria, advisers to private funds with less than \$150 million in AUM are exempt from full registration requirements. However, this \$150 million AUM threshold was too low when it was written in 2010 and it has never been raised nor even indexed for inflation since, notwithstanding the growth of the economy and evolution of the private capital markets since 2010.

Members of this Committee have previously recognized – on a bipartisan basis – that reporting requirements can place a disproportionate burden upon smaller funds. Rep. Barr’s legislation would adjust the \$150 million threshold for inflation since 2010 and annually thereafter. This would ensure that SEC regulation and the universe of registered private fund advisers keeps pace with the growth of the U.S. economy.

Legislation to amend the accredited investor definition

SBIA also supports several bills included for the hearing that would modernize the SEC's definition of an "accredited investor," or individuals eligible to invest in certain private offerings of securities. The current definition equates sophistication with wealth and generally prohibits individuals from investing in private offerings unless they meet minimum income or net worth thresholds. This has the effect of being both overinclusive and underinclusive at the same time – a wealthy person with no knowledge of the financial markets is free to invest in private offerings, while an experienced, sophisticated investor who may not be "wealthy" enough by the SEC's definition is prohibited from doing the same.

The reforms under the Fair Investment Opportunities for Professional Experts, Accredited Investor Definition Review Act, and other bills would expand the definition and permit an individual to demonstrate their financial sophistication and be deemed "accredited," regardless of how much they are worth or how much they make per year. This will help further democratize the financial markets and open up investment opportunities for more households at a time when the private capital markets have substantially grown. Furthermore, it will increase capital access for private businesses that rely on institutions and accredited investors for capital.

SBIA thanks all members for their consideration of these views and looks forward to working with the Financial Services Committee on small business capital formation issues during this Congress.

Sincerely,



Brett Palmer
President
Small Business Investor Alliance