

United States Senate

January 21, 2020

The Honorable Jay Clayton
Chairman
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

Dear Chairman Clayton:

We are writing today to request that you review and update the current definition of a venture capital (VC) fund to more closely align it with developments in the startup ecosystem. We have heard of several developments in venture financings since the definition was finalized in 2011, creating pressure on the ability of many venture capital funds to meet the definition. The consequence of these developments is that VC funds have to choose between passing up investment opportunities and the significant financial burden and complexity of becoming a Registered Investment Advisor (RIA). We would like to work with you to identify these challenges and make certain that the definition of venture capital fund accurately reflects the realities of the industry today.

As you know, the Dodd-Frank Act required that private investment funds register with the Securities and Exchange Commission (SEC) as RIAs. However, the legislation created a separate registration regime for VC funds, recognizing the benefits that the funds provide to the economy. Dodd-Frank required that the SEC adopt an accurate definition of a VC fund, which it finalized in 2011, using a multi-factor test. For example, one of the requirements is that at least 80 percent of a fund's activity must be direct investments into private companies. This test differentiated the VC business model with that of traditional private equity and hedge funds.

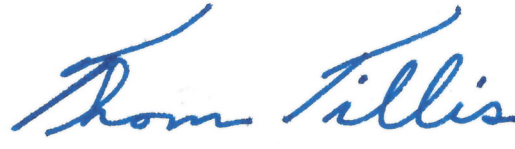
We have noticed that since 2011, trends in industry and our capital markets show that startups and growth companies are staying private longer. This trend has led to an uptick in secondary investments. However, under the current SEC definition, these secondary investments are considered nonqualifying investments. The result of this definition is that these investments fill many VC funds' so-called "baskets" of nonqualifying investment activity, thereby discouraging venture investors from further supporting their portfolio companies. Once a VC fund approaches 20 percent of its activity in secondary or other nonqualifying investments, the fund must make the choice between making further secondary investments in its portfolio companies and taking on the cost and complexity of becoming an RIA, or remaining at Exempt Reporting Adviser status and passing up these opportunities. VC funds should not have to choose between these options, both of which could create adverse economic consequences.


The SEC can address this problem by altering the definition of venture capital to reflect the current state of financing for today's startups. Congress has shown strong bipartisan support for capital formation to this end. Legislation known as the *DEAL Act* passed in the 115th Congress with unanimous support in the House Financial Services Committee and in a bipartisan vote in the full House as a part of the *JOBS and Investor Confidence Act of 2018*.

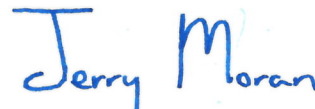
Thank you for your consideration and we look forward to working with you on this issue moving forward.

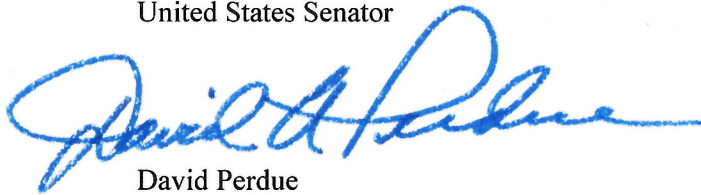
Sincerely,



M. Michael Rounds
United States Senator



Thom Tillis
United States Senator

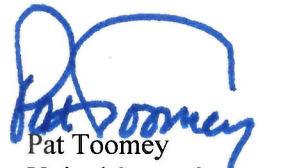

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