

What It Takes to Become an Accredited Investor

For the average investor, the financial landscape can sometimes feel like a complex maze with limited access to certain investment opportunities. However, within this realm exists a distinct category known as accredited investors. If you've ever wondered what sets accredited investors apart, this article provides an overview.

Most investors don't qualify for accredited investor status due to high income level requirements. However, if you can qualify as an accredited investor, you can access additional investment opportunities, which may have more complicated risk/reward characteristics. Join us as we demystify the world of accredited investors, unraveling the meaning, requirements, and potential benefits associated with this designation. Whether you're new to investing or seeking to expand your financial horizons, we'll shed light on what it means to be an accredited investor.

What Is an Accredited Investor?

While businesses and banks can qualify for accredited investments, for the purposes of this article, we'll be discussing what it means to be an accredited investor as an individual.

Despite the formal-sounding title, there is no regulatory board that will certify you as an accredited investor. Regulatory organizations, like the Securities and Exchange Commission (SEC), rely on the due diligence processes of those offering unsecured investments to do the legwork and confirm that their investors qualify as accredited.

For an individual investor to be considered accredited, they must meet the following financial criteria:

- Net worth over \$1 million, excluding their primary residence (individually or with spouse or partner).
- Income over \$200,000 (individually) or \$300,000 (with spouse or partner) in each of the prior two years and reasonably expecting the same for the current year.¹

Investment vehicles looking to determine if someone is an accredited investor will ask for proof. This may come in the form of any available W-2s, other statements of income, credit reports, tax returns, bank accounts and other asset statements, or regulatory credentials (such as a Series 7).²

Pros of Being an Accredited Investor

Meeting the financial requirements to be considered an accredited investor opens up various investment opportunities. Being an accredited investor can allow you to get in on the ground floor of certain investments, but such opportunities also create additional risks.²

Types of investments available to accredited investors include:

- **Private Equity:** Private equity seeks to participate in the growth of private companies. Private equity is also an illiquid asset class that seeks long-term appreciation away from public markets.³
- **Private Placements:** Private placements are sales of equity or debt positions to qualified investors and institutions. This type of investment often serves as an alternative to other approaches that may be taken to raise capital.⁴
- **Hedge Funds:** Hedge funds are investments with broad flexibility in terms of the types of strategies they can employ to follow their stated investment objectives.⁵
- **Venture Capital:** Venture capital represents a form of private equity financing provided by investors to companies looking for capital. This form of financing is primarily directed toward small firms with growth prospects or those that appear to be pursuing rapid expansion.⁶
- **Equity Crowdfunding:** Equity crowdfunding is a business funding model that involves collecting small sums of money from a large number of private investors. However, equity crowdfunding is regulated by the SEC, so businesses soliciting investments in this manner must follow strict guidelines.^{7,8}

Downsides of Being an Accredited Investor

There are several drawbacks when considering an investment as an accredited investor.

- **High Risk:** For example, start-up businesses have high failure rates. While they may appear to offer tremendous potential, you may not recoup your initial investment if you participate.²
- **High Minimum Investment Amounts:** The investment vehicles offered to accredited investors often have high investment requirements. Minimum investments can range as high as several million dollars.²
- **Fees:** Hedge funds, in particular, may have associated fees, such as performance and management fees. A performance fee is paid based on returns on an investment and can range as high as 15% to 20%. This is on top of management fees.⁹
- **Illiquidity Of The Investments:** Many accredited investment vehicles aren't easily made liquid should the need arise. Not only do you risk not recouping your investment, but once you commit to investing, you may not be able to easily access your money.²

Ultimately, accredited investing is for individuals with investment experience who understand the risk/reward profiles of the various associated opportunities.

1. SEC.gov, April 6, 2023
2. Investopedia.com, December 30, 2022
3. Investopedia.com, March 31, 2023
4. Investopedia.com, March 29, 2022
5. Investopedia.com, August 11, 2022
6. Investopedia.com, April 22, 2023
7. Investopedia.com, April 22, 2023

8. Forbes.com, March 31, 2022

9. Investopedia.com, September 29, 2022

The content is developed from sources believed to be providing accurate information. The information in this material is not intended as tax or legal advice. It may not be used for the purpose of avoiding any federal tax penalties. Please consult legal or tax professionals for specific information regarding your individual situation. This material was developed and produced by FMG Suite to provide information on a topic that may be of interest. FMG, LLC, is not affiliated with the named broker-dealer, state- or SEC-registered investment advisory firm. The opinions expressed and material provided are for general information, and should not be considered a solicitation for the purchase or sale of any security. Copyright FMG Suite.