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Financial Services

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Administration Bill Would Require Managers of Hedge and Other Private Funds to Register as Investment Advisers

On July 15, the Obama administration announced proposed legislation entitled the "Private Fund Investment Advisers Registration Act of 2009" that would amend the Investment Advisers Act of 1940 (the "Advisers Act") in a number of ways, with the effect of requiring all U.S.-based investment advisers with more than $30 million in assets under management to register with the SEC. This would affect managers of hedge funds, private equity funds and venture capital funds, and many foreign fund managers that would not fall within narrow exemptive provisions.

The bill would eliminate the "private adviser" exemption currently available to an investment adviser with fewer than 15 clients that neither holds itself out generally to the public as an investment adviser nor acts as an investment adviser to any registered investment company. In place of the private adviser exemption, the bill would create a new exemption for a "foreign private adviser" that (i) has no place of business in the United States; (ii) has fewer than 15 clients in the United States; (iii) has assets under management attributable to clients in the United States of less than $25 million; and (iv) neither holds itself out generally to the public in the United States as an investment adviser, nor acts as an investment adviser to any registered investment company.

The bill would also eliminate for any investment adviser that manages a "private fund": (i) the intrastate exemption from registration available to an investment adviser whose clients are all residents of a single state and who does not furnish advice or issue analyses or reports with respect to securities listed on any national securities exchange, and (ii) the exemption from registration available to an investment adviser that is registered with the CFTC as a CTA whose business does not consist primarily of acting as an investment adviser and that does not act as an investment adviser to any registered investment company. The bill's definition of "private fund" would include hedge funds, private equity funds and other pooled investment vehicles that are excepted from the definition of investment company under Sections 3(c)(1) or 3(c)(7) of the Investment Company Act of 1940, including a fund organized outside the United States if 10% or more of its outstanding securities are held by U.S. persons.

If passed in its current form, a U.S.-based investment adviser with a single client (unless falling under the narrowed intrastate exemption), or that manages a single private fund, would be required to register with the SEC if the investment adviser has more than $30 million under management.

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The bill also proposes to give the SEC the authority to require any registered investment adviser to submit to the SEC reports about the private funds it advises. The reports would require information prescribed by the SEC through rulemaking, which could include, without limitation, assets under management, use of leverage, counterparty credit risk exposures, trading and investment positions and other information deemed necessary or appropriate in the public interest, to protect investors or to assess systemic risk. The bill would require the SEC to consult with the Federal Reserve Board in determining the scope of information to be reported, and would authorize the SEC to make such reports available to the Fed and the Financial Services Oversight Council for purposes of assessing systemic risk and determining if a private fund should be designated a "Tier 1 financial holding company." The reports submitted to the SEC are to be confidential and excepted from application of the Freedom of Information Act.

The proposed amendment would further require that registered investment advisers provide certain reports, records and other documents (to be prescribed by the SEC through rulemaking) to investors, prospective investors, counterparties and creditors of any private fund it advises and specifies that the records of the private fund are deemed records of the investment adviser subject to the recordkeeping requirements of the Advisers Act.

The proposed amendment clarifies the SEC's rulemaking authority to include the ability to determine the new reporting requirements and related definitions, and to ascribe different meanings to terms used in different sections, including the term "client," which the U.S. District for the D.C. Circuit decided in the *Goldstein* decision the SEC did not have legislative authority to so interpret.

Finally, the bill proposes that within six months after the bill is passed, the SEC and the CFTC, after consultation with the Board of Governors of the Federal Reserve System, shall jointly promulgate rules to establish the form and content of reports required to be filed with the SEC and the CFTC by investment advisers that are registered both under the Advisers Act and the Commodity Exchange Act.

The Treasury's proposal appears to be based on the "Private Fund Transparency Act of 2009" introduced in the Senate by Senator Jack Reed on June 16.

To view the text of the bill click here.