

October 29, 2009

PRIVATE EQUITY DEVELOPMENTS

House Committee Approves Private Fund Adviser Registration Bill

On Tuesday, by a vote of 67-1, the Financial Services Committee of the House of Representatives approved the Private Fund Investment Advisers Registration Act, sending it to the full House. The bill would require most private equity and hedge fund managers to register with the SEC under the Investment Advisers Act of 1940 ("IAA").

The bill proposes to eliminate the "private adviser" exemption from the IAA, thus requiring that an "investment adviser who acts as an investment adviser to any private fund" register with the SEC, subject to a new threshold that such adviser have at least \$150 million of assets under management. Although the bill excludes from registration "venture capital firms" (as will be defined by the SEC) and investment advisers managing less than \$150 million of assets, even these advisers would have to maintain records and provide annual reports to the SEC. The bill would also exempt from registration certain "foreign private fund advisers" that have no place of business in the U.S., manage less than \$25 million attributable to U.S. clients and have fewer than 15 U.S. clients.

Under the bill, investment advisers must report to the SEC for each private fund they advise "the amount of assets under management, use of leverage (including off-balance sheet leverage), counterparty credit risk exposures, trading and investment positions, and trading practices," along with other information "necessary or appropriate in the public interest and for the protection of investors or for the assessment of systemic risk." The SEC may share this information with the Federal Reserve or any other entity that has responsibility for monitoring systemic risk. The SEC is granted authority to define the technical terms in the bill, as well as broad rulemaking authority to establish varying compliance standards based on fund size and type.

Currently, the IAA generally prohibits the SEC from requiring "any investment adviser engaged in rendering investment supervisory services to disclose the identity, investments, or affairs of any client of such investment adviser." The bill eliminates this provision, potentially enabling the SEC to compel disclosure of confidential client information.

The bill contains few surprises in light of the white paper, "Financial Regulatory Reform - A New Foundation: Rebuilding Financial Supervision and Regulation," released by the Department of the Treasury in mid-June. We expect that some form of the bill will ultimately be approved and signed into law. Once the bill is passed, investment advisers would not be required to register until one year after enactment of the legislation. Investment advisers of most private equity and hedge funds should anticipate registering with the SEC, enhancing reporting and recordkeeping, allowing broad access to records, and establishing compliance procedures.

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