

ADVISORY | Private Funds

November 14, 2011

SEC ADOPTS FINAL RULES REQUIRING REPORTING BY PRIVATE FUND ADVISERS

On October 26, 2011, the Securities and Exchange Commission (the “SEC”) adopted Rule 204(b)-1 under the Investment Advisers Act of 1940, as amended (the “Advisers Act”), which requires certain advisers to private funds to report on a new Form PF information on the basic operations and strategies of the private funds they manage.¹ Form PF is intended to assist the Financial Stability Oversight Commission (the “FSOC”) (established under the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”)) in assessing the systemic risk posed by investments in private funds. In this client advisory, we discuss the notable aspects of Form PF and reporting impact for advisers to private funds.

WHO MUST FILE FORM PF

Rule 204(b)-1 requires an adviser to file with the SEC (electronically via the Investment Adviser Registration Depository) a Form PF if the adviser (1) is registered or required to be registered under the Advisers Act, (2) advises one or more private funds,² and (3) had at least \$150 million in regulatory assets under management (described below) as of the end of its most recently completed fiscal year. Exempt advisers, including those that satisfy the venture capital fund exemption or the exemption for advisers to private funds with less than \$150 million in assets under management, need not file the form.

Scaled Approach to Reporting – Small and Large Private Fund Advisers

The amount of information required to be reported on Form PF and the frequency of such reporting depends on the class to which the adviser belongs and the types of private funds it manages. Most private fund advisers only will be required to complete section 1 of Form PF, furnishing information on the adviser’s identity and assets under management, as well as on the size, leverage, and performance of all private funds subject to the reporting requirements. Form PF imposes additional disclosure obligations on three groups of “large private fund advisers”:

- **Large Hedge Fund Advisers.** Advisers with at least \$1.5 billion in regulatory assets under management attributable to “hedge funds”³ as of the end of any month in the prior fiscal quarter

¹ See Reporting by Investment Advisers to Private Funds and Certain Commodity Pool Operators and Commodity Trading Advisers on Form PF, SEC Release No. IA-3308 (Oct. 31, 2011) (available [here](#)).

² A “private fund” is an issuer that would be an investment company but for the exemptions in Section 3(c)(1) or 3(c)(7) of the Investment Company Act of 1940, as amended (the “Company Act”). In general, Form PF classifies seven types of private funds: (1) hedge funds; (2) liquidity funds; (3) private equity funds; (4) real estate funds; (5) securitized asset funds; (6) venture capital funds; and (7) other private funds.

³ Form PF defines a “hedge fund” as a private fund (other than a securitized asset fund) having any one of three common characteristics of a hedge fund: (1) a performance fee that takes into account market value (instead of only realized gains); (2) borrowing an amount in excess of one half of the fund’s net asset value (including any committed capital) or having gross notional exposure in excess of twice its net asset value (including any committed capital); or (3) short selling (other than for hedge currency exposure or managing duration). For purposes of Form PF, any commodity pool upon which an adviser is required to report is

(“Large Hedge Fund Advisers”) must complete section 2 of Form PF. Under this section, Large Hedge Fund Advisers must report aggregate information about the hedge funds managed by such advisers. Large Hedge Fund Advisers must provide fund-specific data for any managed hedge fund with a net asset value of at least \$500 million as of the end of any month in the prior fiscal quarter, including information on the fund’s portfolio liquidity, holdings of unencumbered cash, counterparty credit exposure, and concentration of positions.

- *Large Liquidity Fund Advisers.* Advisers with at least \$1 billion in combined regulatory assets under management attributable to liquidity funds and registered money market funds⁴ as of the end of any month in the prior fiscal quarter (“Large Liquidity Fund Advisers”) must complete section 3 of Form PF. This section requires information on each liquidity fund’s portfolio valuation and valuation methodology, as well as the liquidity of the fund’s holdings.
- *Large PE Fund Advisers.* Advisers with at least \$2 billion in regulatory assets under management attributable to private equity funds⁵ as of the last day of the adviser’s most recently completed fiscal year (“Large PE Fund Advisers”) must complete section 4 of Form PF. Large PE Fund Advisers must report information on each private equity fund they manage, including bridge financing and the leverage of the portfolio companies that the fund controls.

CALCULATING REGULATORY ASSETS UNDER MANAGEMENT

Many of Form PF’s thresholds are dependent on an adviser’s “regulatory assets under management,” which is calculated the same way as it is under Form ADV. Advisers must perform this calculation on a gross basis, without any deductions for outstanding debts or accrued but unpaid liabilities. For private funds advisers, regulatory assets under management include the value of any private fund, regardless of the number of assets held by the fund, and any uncalled capital commitments. Assets must be valued at their market value, or at fair value, if market value is not attainable.

In determining whether an adviser (1) meets the \$150 million minimum threshold or (2) is a large private fund adviser, the adviser generally must aggregate the assets of its parallel managed accounts (i.e., managed accounts that pursue substantially the same investment objective and strategy and invest in substantially the same position as private funds advised by the firm), unless the value of those accounts is greater than the value of the private funds with which they are managed. Additionally, an adviser must aggregate the assets of private funds advised by any “related persons”⁶ except if the adviser would not be required to complete section 7.A. of Schedule D to Form ADV in respect of the related person.⁷

categorized as a hedge fund. The implications of Form PF for advisers to commodity pool operators and commodity trading advisors is beyond the scope of this client advisory.

⁴ Form PF, a “liquidity fund” is any private fund that seeks to generate income by investing in a portfolio of short term obligations in order to maintain a stable net asset value per unit or minimize principal volatility for investors. A “money market fund” is defined by reference to Rule 2a-7 under the Company Act.

⁵ Form PF defines “private equity fund” as any private fund that is not a hedge fund, liquidity fund, real estate fund, securitized asset fund or venture capital fund and does not provide investors with redemption rights in the ordinary course.

⁶ “Related person” is defined generally as: (1) all of the adviser’s officers, partners, or directors (or any person performing similar functions); (2) all persons directly or indirectly controlling, controlled by, or under common control with the adviser; and (3) all of the adviser’s employees (other than employees performing only clerical, administrative, support or similar functions).

⁷ Section 7.A. of Schedule D to Form ADV would not be required with respect to a related person if (1) the adviser has no business dealings with the related person in connection with advisory services provided to clients; (2) the adviser does not conduct shared operations with the related person; (3) the adviser does not

If an adviser's principal office and place of business is outside of the United States, the adviser may exclude any private fund that, during the last fiscal year, was not, and was not beneficially owned by, a United States person and was not offered in the United States. An adviser also may exclude any assets invested in the equity of other private funds.

Frequency of Testing

As proposed, Rule 204(b)-1 would have required advisers to hedge and liquidity funds to determine whether they crossed the thresholds described above on a daily basis. Advisers to private equity funds would have been required to make a quarterly assessment. Now, however, advisers need only test whether their hedge fund or liquidity fund assets meet the applicable thresholds on a monthly basis, while advisers to private equity funds must test annually whether they meet Form PF's thresholds.

REPORTING FREQUENCY

The following Form PF reporting deadlines are applicable to private fund advisers:

- Small private fund advisers and Large PE Fund Advisers must file Form PF on an annual basis within 120 days after the end of each fiscal year;
- Large Liquidity Fund Advisers must file Form PF within 15 days after each quarter end; and
- Large Hedge Fund Advisers must file Form PF within 60 days after quarter end.

Large private fund advisers with quarterly filing obligations must complete quarterly filings for the type of fund they manage that exceeds the large private fund adviser threshold. For example, a Large Liquidity Fund Adviser that also manages a portfolio of private equity fund assets worth more than \$2 billion must file quarterly reports with respect to its liquidity funds, but only must include information on its private equity funds when it files Form PF for its fourth quarter. In this case, the Large Liquidity Fund Adviser could file a Form PF with respect to its liquidity and registered money market funds under management within 15 days of its quarter end and then amend its Form PF within 120 days after the end of its fourth quarter to include information on the private equity funds it manages.

FLEXIBILITY IN REPORTING

For structurally complex private fund advisers, Form PF permits some measure of reporting flexibility to facilitate clearer disclosures. For instance, an adviser may, but is not required to, report the private fund assets that it manages and the private fund assets that its related persons manage on a single Form PF. Also, an adviser may provide information regarding master-feeder arrangements and parallel fund structures in the aggregate or separately, provided that it does so consistently throughout the Form. The form permits advisers to rely on their own internal methodologies and the conventions of their service providers in reporting information, provided the information is consistent with information that they report internally and to current and prospective investors. To this end, the SEC also removed from Form PF proposed certification language, which would have required an authorized individual to affirm "under penalty of perjury" that the statements made in the form are

refer clients or business to the related person, and vice versa; (4) the adviser does not share clients or premises with the related person; and (5) the adviser has no reason to believe that its relationship with the related person creates a conflict of interest with its clients.

“true and correct.” The removal of such language should permit advisers to exercise a greater degree of judgment in preparing responses to Form PF’s prompts.

CONFIDENTIALITY

Due to the sensitivity of the information solicited by Form PF, the SEC indicated that it does not intend to make public Form PF information identifiable to any particular adviser or private fund, but may use the information in connection with an enforcement action. The SEC will make information collected through Form PF available to the FSOC and to other federal departments, regulatory agencies or SROs for purposes within the scope of their jurisdiction, subject to confidentiality provisions within the Dodd-Frank Act.

COMPLIANCE DATES

There will be a two-step phase-in period for compliance with Form PF’s filing requirements. Most private fund advisers must file their first Form PF following the end of their first fiscal year or fiscal quarter, as applicable, to end on or after December 15, 2012. A more limited subset of private fund advisers must begin filing Form PF following the end of their first fiscal year or fiscal quarter, as applicable, to end on or after June 15, 2012:

- Large Hedge Fund Advisers with at least \$5 billion in assets under management attributable to hedge funds;
- Large Liquidity Fund Advisers with at least \$5 billion in combined assets under management attributable to liquidity funds and registered money market funds; and
- Large Private Equity Fund Advisers with at least \$5 billion in assets under management attributable to private equity funds.

CONCLUSION

As discussed above, Form PF requires certain private fund advisers to provide to the SEC substantial information about the different private funds they manage. While these reporting obligations are not immediate, there is no time like the present for private fund advisers to become accustomed to the various aspects of Form PF and to ensure that they have the systems in place to collect the relevant information.

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