

Client Alert

Latham & Watkins
Corporate Department

Proposed Form PF Would Require Significant Additional SEC Reporting by Fund Sponsors

On January 25, 2011, the Securities and Exchange Commission (SEC) proposed new Rule 204(b)-1 under the Investment Advisers Act of 1940 (Advisers Act), which would require registered investment advisers to make periodic filings on new Form PF with the SEC. The proposed rule, along with a companion rule under the Commodity Exchange Act, has been jointly proposed by the SEC and the Commodity Futures Trading Commission to implement provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act, enacted July 21, 2010 (Dodd-Frank). These proposed rules are designed to assist the Financial Stability Oversight Council (FSOC) created by Dodd-Frank in assessing potential systemic threats to the financial stability of the United States arising from private fund activities. Managers of private equity funds, real estate funds, hedge funds and liquidity funds (i.e., unregistered money market funds) would be affected.

Proposed Rule 204(b)-1 would require substantial new periodic disclosures by all affected investment advisers. The rule is designed to require more detailed information from larger advisers than from smaller advisers, and more information from hedge fund advisers than from private equity fund advisers. The proposed differences are based on

the SEC's assessment of varying levels of systemic risk associated with the different activities undertaken by these advisers. Below is a high-level summary of proposed Rule 204(b)-1, with a focus on the rule as applied to private equity fund advisers.

Proposed Rule 204(b)-1

Who is Affected. Proposed Rule 204(b)-1 would impose reporting obligations on "private fund advisers," defined as any investment adviser registered or required to register with the SEC that advises one or more private funds. A "private fund" is defined as an issuer that would be an investment company under the Investment Company Act of 1940 but for Section 3(c)(1) or 3(c)(7) of that Act. The rule would exempt from any Form PF requirements those investment advisers that are exempt from registration under the Advisers Act, including advisers to venture capital funds, advisers to private funds with less than \$150 million in assets under management in the United States and advisers availing themselves of the "foreign private adviser" exemption.¹ Form PF requirements would also not apply to those investment advisers whose funds rely solely on Section 3(c)(5)(C) for purposes of the Investment Company Act of 1940.²

"As proposed, new Rule 204(b)-1 would require significant disclosures to be made by private fund advisers, and particularly Large Private Fund Advisers."

Reporting Obligations. All private fund advisers would be required to complete certain basic information on Form PF. Private fund advisers with \$1 billion or more in qualifying private equity fund, hedge fund and liquidity fund assets under management (Large Private Fund Advisers) would be required to complete additional information on Form PF based on fund type. Large Private Fund Advisers would be required to update their Form PF filings on a quarterly basis, while all other filers would be required to update their filings annually. For purposes of determining assets under management, private fund advisers would be required to aggregate amounts managed directly with (i) amounts managed by the adviser's "related persons" and (ii) assets held in managed accounts that pursue substantially the same investment objective and strategy and invest in substantially the same positions as one of the adviser's private funds. "Related persons" include the management team of the adviser and all persons or entities directly or indirectly controlling, controlled by or under common control with the adviser.

Form PF Content. Form PF would require all private fund advisers to disclose their assets under management (including certain breakdowns thereof) and other fund-specific data, including:

- Gross and net asset value of each private fund
- Monthly and quarterly fund performance data
- Each private fund's total borrowings, along with a breakdown of the fund's borrowings among domestic and international financial institutions and non-financial institutions

- Identities of creditors to which any of the adviser's funds owes an amount equal to at least 5 percent of such fund's net asset value
- Total number of beneficial owners
- Percentage ownership of the five beneficial owners having the largest equity interests in the fund

Large Private Fund Advisers would be required to provide additional reporting, the focus of which would depend on the type of fund advised. Large Private Fund Advisers to private equity funds³ would be required to report additional detailed information about each private equity fund under management, including the following:

- Information about fund borrowings and guarantees
- Information about debt of controlled portfolio companies (including debt-to-equity ratios and debt maturity profiles)
- Identity of persons providing bridge financing to portfolio companies and the amount of such financing
- Additional information regarding financial industry portfolio companies
- Information on events of default on any fund debt or portfolio company debt during the reporting period
- A breakdown of the fund's investments by industry and geography

Filing Frequency. The SEC anticipates that the proposed rule would have an initial compliance date of December 15, 2011 (the Effective Date). Proposed reporting deadlines are set forth below. The proposed rule would also require that advisers pay as-yet-undetermined filing fees in connection with Form PF filings.

Category of Adviser	Filing Obligation
Private Fund Advisers (Excluding Large Private Fund Advisers)	<ul style="list-style-type: none"> • First filing due within 90 days after end of adviser's first fiscal year ending on or after the Effective Date • Annual updates due within 90 days after end of each subsequent fiscal year
Large Private Fund Advisers	<ul style="list-style-type: none"> • First filing due January 15, 2012 • Quarterly updates due within 15 days after end of each subsequent calendar quarter
Advisers Registering After the Effective Date	<ul style="list-style-type: none"> • Initial filing due within 15 days after end of the next occurring calendar quarter following registration • Subsequent filings in accordance with the above

Disclosure of Form PF Information. The SEC has indicated that it does not intend to make filed Form PF information publicly available, but the SEC would nevertheless make such information available to the FSOC for evaluation of systemic risk consistent with the requirements of Dodd-Frank. The SEC has stated that it also expects to share Form PF information on a confidential basis with foreign financial regulators and that it may also disclose such information to other federal departments and agencies, to self-regulatory organizations or pursuant to certain court orders. Information collected on Form PF would also be used by the SEC in its own regulatory programs, including for purposes of examinations and enforcement actions.

Recordkeeping Requirements. The SEC has indicated that it will address additional recordkeeping requirements specific to private fund advisers for systemic risk assessment purposes in a separate release.

Comment Period. The SEC is currently accepting comments on the proposed rule. The comment period will end 60 days following publication of the proposed rule in the Federal Register.

Conclusion

As proposed, new Rule 204(b)-1 would require significant disclosures to be made by private fund advisers, and particularly Large Private Fund Advisers. This enhanced disclosure obligation, particularly for Large Private Fund Advisers, would require disclosure of information typically considered proprietary to an investment adviser's operations. We will continue to monitor the regulatory process with respect to these proposals.

Endnotes

¹ Dodd Frank eliminated the broad-based “private adviser” exemption on which many private fund advisers previously relied.

² Section 3(c)(5)(C) provides an exemption from “investment company” status under the Investment Company Act of 1940 for certain real estate funds that are primarily engaged in purchasing or otherwise acquiring mortgages and other liens on and interest in real estate.

³ A “private equity fund” is defined as any private fund that is not a hedge fund, liquidity fund, real estate fund, securitized asset fund or venture capital fund and which does not provide investors with redemption rights in the ordinary course.

A “hedge fund” is defined to include private funds that have any one of what the SEC cites in the proposing release as the “three common characteristics of a hedge fund: a performance fee using market value (instead of only realized gains), high leverage or short selling.” Private equity funds with any of these characteristics may therefore be classified as hedge funds under the proposed rule.

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