

FACT SHEET**Dodd-Frank Act Amendments to the Investment Advisers Act****Background**

A large number of individuals and institutions invest a significant amount of assets in private funds, such as hedge funds and private equity funds. However, until the passage of the Dodd-Frank Act, advisers managing those assets were subject to little regulatory oversight.

With the Dodd-Frank Act, Congress closed this regulatory gap by generally extending the registration requirements under the Investment Advisers Act to the advisers of these funds. The new law also provided the Commission with the ability to require the limited number of advisers to private funds that will not have to register to file reports about their business activities.

Further, in acknowledging the Commission's limited examination resources – and in light of the new responsibilities for private fund advisers – the Dodd-Frank Act reallocated regulatory responsibility for certain mid-sized investment advisers to the state securities authorities.

Private Fund Advisers and Commission Registration

For many years, advisers to private funds have been able to avoid registering with the Commission because of an exemption that applies to advisers with fewer than 15 clients – an exemption that counted each fund as a client, as opposed to each investor in a fund. As a result, some advisers to hedge funds and other private funds have remained outside of the Commission's regulatory oversight even though those advisers could be managing large sums of money for the benefit of hundreds of investors.

Title IV of the Dodd-Frank Act eliminated this private adviser exemption. Consequently, many previously unregistered advisers, particularly those to hedge funds and private equity funds, will have to register with the Commission and be subject to its regulatory oversight, rules and examination.

These advisers will be subject to the same registration requirements, regulatory oversight, and other requirements that apply to other SEC-registered investment advisers. To provide these advisers with a window to meet their new obligations, the transition provisions the Commission is adopting today will require these advisers to be registered with the Commission by March 30, 2012.

Reporting Requirements for Hedge Fund and Other Investment Advisers*Background*

When investment advisers register with the Commission, they provide information in their registration form that is not only used for registration purposes, but that is used by the Commission in its regulatory program to support its mission to protect investors.

To enhance its ability to oversee investment advisers to private funds, the Commission is requiring advisers to provide additional information about the private funds they manage. The information obtained as a result of these amendments will assist the Commission in fulfilling its increased responsibility for private fund advisers arising from the Dodd-Frank Act.

The Form

Under the amended adviser registration form, advisers to private funds will have to provide:

- Basic organizational and operational information about each fund they manage, such as the type of private fund that it is (e.g., hedge fund, private equity fund, or liquidity fund), general information about the size and ownership of the fund, general fund data, and the adviser's services to the fund.
- Identification of five categories of "gatekeepers" that perform critical roles for advisers and the private funds they manage (i.e., auditors, prime brokers, custodians, administrators and marketers).

These reporting requirements are designed to help identify practices that may harm investors, deter advisers' fraud, and facilitate earlier discovery of potential misconduct. And this information will provide for the first time a census of this important area of the asset management industry.

In addition, the Commission is adopting other amendments to the adviser registration form to improve its regulatory program. These amendments will require all registered advisers to provide more information about their advisory business, including information about:

- The types of clients they advise, their employees, and their advisory activities.
- Their business practices that may present significant conflicts of interest (such as the use of affiliated brokers, soft dollar arrangements and compensation for client referrals).

The rules also will require advisers to provide additional information about their non-advisory activities and their financial industry affiliations.

Reporting Requirements for Exempt Advisers

Background

While many private fund advisers will be required to register, some of those advisers may not need to if they are able to rely on one of three new exemptions from registration under the Dodd-Frank Act, including exemptions for:

- Advisers solely to venture capital funds.
- Advisers solely to private funds with less than \$150 million in assets under management in the U.S.
- Certain foreign advisers without a place of business in the U.S.

The Commission can still impose certain reporting requirements upon advisers relying upon either of the first two of these exemptions ("exempt reporting advisers").

The Rules

Under the new rules, exempt reporting advisers will nonetheless be required to file, and periodically

update, reports with the Commission, using the same registration form as registered advisers.

Rather than completing all of the items on the form, exempt reporting advisers will fill out a limited subset of items, including:

- Basic identifying information for the adviser and the identity of its owners and affiliates.
- Information about the private funds the adviser manages and about other business activities that the adviser and its affiliates are engaged in that present conflicts of interest that may suggest significant risk to clients.
- The disciplinary history (if any) of the adviser and its employees that may reflect on the integrity of the firm. Exempt reporting advisers will file reports on the Commission's investment adviser electronic filing system (IARD), and these reports will be publicly available on the Commission's website. These advisers will be required to file their first reports in the first quarter of 2012.

Reallocation of Regulatory Responsibility

Background

Since 1996, regulatory responsibility for investment advisers has been divided between the Commission and the states, primarily based on the amount of money an adviser manages for its clients. Under existing law, advisers generally may not register with the Commission unless they manage at least \$25 million for their clients.

The Dodd-Frank Act raises the threshold for Commission registration to \$100 million by creating a new category of advisers called "mid-sized advisers." A mid-sized adviser, which generally may not register with the Commission and will be subject to state registration, is defined as an adviser that:

- Manages between \$25 million and \$100 million for its clients.
- Is required to be registered in the state where it maintains its principal office and place of business.
- Would be subject to examination by that state, if required to register.

As a result of this amendment to the Investment Advisers Act, about 3,200 of the current 11,500 registered advisers will switch from registration with the Commission to registration with the states. These advisers will continue to be subject to the Advisers Act's general anti-fraud provisions.

The Rules

The Commission is adopting amendments to several of its current rules and forms to:

- Reflect the higher threshold required for Commission registration.
- Provide a buffer to prevent advisers from having to frequently switch between Commission and state registration.

- Clarify when an adviser will be a mid-sized adviser.
- Facilitate the transition of advisers between federal and state registration in accordance with the new requirements. Advisers registered with the Commission will have to declare that they are permitted to remain registered in a filing in the first quarter of 2012, and those no longer eligible for Commission registration will have until June 28, 2012 to complete the switch to state registration.

Pay-to-Play

The Rule

The Commission also is amending the investment adviser “pay-to-play” rule in response to changes made by the Dodd-Frank Act. The pay to play rule is designed to prevent an adviser from seeking to influence government officials’ awards of advisory contracts through political contributions.

Under the amendment, an adviser will be permitted to pay a registered municipal advisor to act as a placement agent to solicit government entities on its behalf, if the municipal advisor is subject to a pay-to-play rule adopted by the MSRB that is at least as stringent as the investment adviser pay-to-play rule. The MSRB received new authority over municipal advisors under the Dodd-Frank Act. Advisers will also continue to be permitted to hire as a placement agent an SEC registered investment adviser or a broker-dealer that is subject to a pay-to-play rule adopted by FINRA that is at least as stringent as the investment adviser pay-to-play rule.

* * *

Exemptions for Advisers to Venture Capital Funds, Private Fund Advisers With Less Than \$150 Million in Assets Under Management, and Foreign Private Advisers

Background

As previously described, the Dodd-Frank Act eliminated the private adviser exemption and created three new exemptions for:

- Advisers solely to venture capital funds.
- Advisers solely to private funds with less than \$150 million in assets under management in the United States.
- Certain foreign advisers without a place of business in the United States.

The Commission is adopting rules that would implement these exemptions and define various terms.

New Exemptions

Definition of Venture Capital Fund

The Dodd-Frank Act amended the Advisers Act to exempt from registration advisers that only manage venture capital funds, and directed the Commission to define the term “venture capital fund.” The Commission is adopting a definition of “venture capital fund” that is designed to effect Congress’

intent in enacting this exemption.

Under the definition, a venture capital fund is a private fund that:

- Invests primarily in “qualifying investments” (generally, private, operating companies that do not distribute proceeds from debt financings in exchange for the fund’s investment in the company); may invest in a “basket” of non-qualifying investments of up to 20 percent of its committed capital; and may hold certain short-term investments.
- Is not leveraged except for a minimal amount on a short-term basis.
- Does not offer redemption rights to its investors.
- Represents itself to investors as pursuing a venture capital strategy.

Under a grandfathering provision, funds that began raising capital by the end of 2010 and represented themselves as pursuing a venture capital strategy would generally be considered venture capital funds. The Commission is adopting this approach because it could be difficult or impossible for advisers to conform these pre-existing funds, which generally have terms in excess of 10 years, to the new definition.

Private Fund Advisers With Less Than \$150 Million in Assets Under Management in U.S.

The Commission also is adopting a rule that would implement the new statutory exemption for private fund advisers with less than \$150 million in assets under management in the United States. The rule largely tracks the provision of the statute.

Foreign Private Advisers

The Dodd-Frank Act also amended the Advisers Act to provide for an exemption from registration for foreign advisers that do not have a place of business in the United States, and have:

- Less than \$25 million in aggregate assets under management from U.S. clients and private fund investors.
- Fewer than 15 U.S. clients and private fund investors.

The Commission is adopting rules to define certain terms included in the statutory definition of “foreign private adviser” in order to clarify the application of the foreign private adviser exemption and reduce the potential burdens for advisers that seek to rely on it. The rule incorporates definitions set forth in other Commission rules, all of which are likely to be familiar to foreign advisers active in the U.S. capital markets.

<http://www.sec.gov/news/press/2011/2011-133.htm>