

SEC AND CFTC ADOPT PRIVATE FUND REPORTING RULES

AGENCIES ADOPT NEW FORM PF

Effective October 31, 2011, the Securities and Exchange Commission and the Commodity Futures Trading Commission adopted new risk reporting rules that require registered advisers to various private funds to report, on a confidential basis, certain data to the SEC (“Form PF Release”).¹ Information collected under the new reporting regime is intended to provide empirical data to the Financial Stability Oversight Council that it may use in assessing and monitoring the extent to which activities of certain private funds and their advisers pose systemic risk to the U.S. financial system. Both the SEC and CFTC may use the data collected on Form PF in their regulatory programs, including examinations, investigations and investor protection efforts. Click here for a link to [Form PF](#).

A. Who Must File Form PF

Rule 204(b)-1 under the Investment Advisers Act requires any registered investment adviser that advises one or more “private funds” and has at least \$150 million in regulatory assets under management (“RAUM”)² attributable to private funds to file Form PF with the SEC. Also, any adviser that is registered with the CFTC as a commodity pool operator (a “CPO”) or a commodity trading advisor (a “CTA”), is also registered with the SEC as an investment adviser and has at least \$150 million in RAUM is required to file Form PF with the SEC. A private fund is generally defined as a fund relying on an exclusion from the definition of an investment company provided by either Section 3(c)(1) or 3(c)(7) of the Investment Company Act of 1940, as amended (the “1940 Act”). In total, there are seven types of private funds defined in Form PF: (1) hedge fund; (2) liquidity fund; (3) private equity fund; (4) real estate fund; (5) securitized asset fund; (6) venture capital fund; and (7) other private fund. Form PF generally requires more information about hedge funds than other types of private funds.

Private fund advisers are divided into two groups on the basis of their RAUM for purposes of determining the amount and frequency of information to be reported by the adviser on Form PF. The first group is comprised of smaller private fund advisers; these advisers must have at least \$150 million in RAUM attributable to private funds. The second group consists of large private fund advisers that advise hedge, liquidity or private equity funds.

¹ See *Reporting by Investment Advisers to Private Funds and Certain Commodity Pool Operators and Commodity Trading Advisors on Form PF*, IA-3308 (Oct. 31, 2011) (adopting Rule 204(b)-1 under the Investment Advisers Act of 1940, as amended (the “Investment Advisers Act”)), available at <http://sec.gov/rules/final/2011/ia-3308.pdf>. See also our client memoranda “[SEC Adopts Private Fund Reporting Rules and Form PF](#)” (Oct. 27, 2011) and “[SEC and CFTC Propose Private Fund Reporting Rules; Agencies Introduce New Forms PF, CPO-PQR and CTA-PR; CFTC Proposes to Limit Registration Exemptions](#)” (Feb. 28, 2011).

² The RAUM definition, which was recently adopted in connection with amendments to the SEC’s Form

a. Smaller Private Fund Advisers

“Smaller private fund advisers” include advisers registered or required to be registered with the SEC that advise private funds with at least \$150 million in RAUM but do not fall within any of the categories of large private fund adviser discussed below. Unlike large private fund advisers, smaller private fund advisers are required to file Form PF once a year and to report only the basic information about their private funds that is required of all Form PF filers (with some additional information for hedge fund advisers), as described in more detail below under “What Information Must Be Provided on Form PF?”

b. Large Private Fund Advisers

There are three types of “large private fund advisers” that are required to complete certain additional sections of Form PF: (1) those with at least \$1.5 billion in RAUM attributable to hedge funds (defined below) as of the last day of any month in the fiscal quarter immediately preceding the most recently completed fiscal quarter; (2) those managing a liquidity fund (defined below) with at least \$1 billion in combined RAUM attributable to liquidity funds and registered money market funds as of the last day of any month in the fiscal quarter immediately preceding the most recently completed fiscal quarter; and (3) those with at least \$2 billion in RAUM attributable to private equity funds as of the last day of the adviser’s most recently completed fiscal year.

i. *Large Hedge Fund Advisers*

Form PF defines³ “hedge fund” to include any private fund (other than a securitized asset fund): (a) with respect to which one or more investment advisers (or related persons of investment advisers) may be paid a performance fee or allocation calculated by taking into account unrealized gains (other than a fee or allocation the calculation of which may take into account unrealized gains solely for the purpose of reducing such fee or allocation to reflect net unrealized losses); (b) that may borrow an amount in excess of one-half of its net asset value (including any committed capital) or may have gross notional exposure in excess of twice its net asset value (including any committed capital); or (c) that may sell securities or other assets short or enter into similar transactions (other than for the purpose of hedging currency exposure or managing duration). Solely for purposes of Form PF, a commodity pool that is required to be reported on Form PF is treated as a hedge fund.

ii. *Large Liquidity Fund Advisers*

Form PF defines “liquidity fund” as 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 (*e.g.*, unregistered money market funds). An adviser to liquidity funds must combine liquidity fund and registered money market fund assets under management for purposes of determining whether the adviser meets the threshold for being a

³ Form PF, like Form ADV, has defined terms in italics and defines such terms in a glossary. The glossary is at the end of Form PF.

large liquidity fund adviser. However, such an adviser would only have to report information about the unregistered liquidity funds on Form PF.⁴

iii. *Large Private Equity Fund Advisers*

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.

B. When to File Form PF

a. General Filing Requirements

All registered advisers with at least \$150 million in RAUM attributable to private funds, including all large private equity fund advisers but not large hedge fund advisers or large liquidity fund advisers, are required to file Form PF on an annual basis, within 120 days of the end of the fiscal year. The filing requirements for the three categories of large private fund advisers are as follows:

Type of Large Private Fund Adviser:	Filing Frequency:
Hedge fund adviser with at least \$1.5 billion in RAUM	Quarterly: within 60 days of the end of each fiscal quarter
Liquidity fund adviser with at least \$1 billion in RAUM	Quarterly: within 15 days of the end of each fiscal quarter
Private equity fund adviser with at least \$2 billion in RAUM	Annually: within 120 days of the end of the fiscal year

It is important to note that unlike under the proposed rule, under the final rule a private fund adviser that is required to report on a quarterly basis (*i.e.*, a large hedge fund adviser) will have to report only in relation to the type of private fund that caused that adviser to exceed the reporting threshold. Thus, an adviser will not have to file quarterly reports in relation to private equity funds, venture capital funds or real estate funds that the adviser also manages.⁵

b. Initial Filing Deadlines

The agencies have adopted a tiered phase-in period for initial filings. The majority of private fund advisers will be required to file Form PF within the time frames noted in the table above after the first fiscal year or fiscal quarter, as applicable, ending on or after December 15, 2012. A private fund adviser with at least \$5 billion in RAUM, however, must file its initial Form PF after the first fiscal year or fiscal quarter, as applicable, ending on or after June 15, 2012. Thus, while most private fund advisers will be required to file their first Form PF in 2013, some

⁴ See Form PF Release, *supra* note 1, at 34.

⁵ See *Id.* at 54.

advisers will have to file in the latter part of 2012. For example, an adviser that has \$5 billion in RAUM attributable to hedge funds as of March 31, 2012, will have to file its first Form PF within 60 days following June 30, 2012.⁶

C. Aggregating Assets Under Management

In order to determine whether an adviser meets the \$150 million minimum reporting threshold or the large private fund adviser threshold, the adviser must aggregate (a) assets of managed accounts advised by the firm that pursue substantially the same investment objective and strategy and invest side by side in substantially the same positions as the private funds advised by the adviser (“parallel managed accounts”), unless the value of those accounts exceeds the value of the private funds which they parallel; and (b) assets of private funds advised by any of the adviser’s “related persons” other than related persons that are separately operated.

While the agencies modified the aggregation requirements contained in the proposed rule to give an adviser the ability to exclude under the circumstances noted above,⁷ it expressed concern that advisers focusing on private funds “may increasingly structure investments as separate accounts to avoid Form PF reporting requirements . . .”⁸ The agencies cautioned that “advisers, as fiduciaries, may not subordinate clients’ interests to their own such as by altering the structure of investments in a way that is not in the client’s best interest in an attempt to remain under reporting thresholds.”⁹

Under the final rule an adviser is permitted to exclude assets under management that are attributable to “related persons”¹⁰ that are separately operated. Instructions to Section 7.A. of Schedule D to Form ADV provide that a related person is separately operated from an adviser if (1) the adviser has no business dealings with the related person in connection with advisory services provided to its clients; (2) the adviser does not conduct shared operations with the related person; (3) the adviser does not refer clients or business to the related person, and the related person does not refer prospective clients or business to the adviser; (4) the adviser does not share supervised persons or premises with the related person; and (5) the adviser has no reason to believe that its relationship with the related person otherwise creates a conflict of interest with its clients.¹¹

⁶ See *Id.* at 117-118.

⁷ See *Id.* at 42.

⁸ See *Id.* at 43.

⁹ See *Id.* at 43, n.121.

¹⁰ Form PF defines related person, by incorporating the definition in Form ADV, 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).”

¹¹ See Form PF Release, *supra* note 1, at 45, n.127.

Advisers are instructed to disregard any private fund's equity investments in other private funds for purposes of both reporting thresholds and responding to questions on Form PF.¹² In addition, if an adviser to a fund of funds invests substantially all of that fund's assets in the equity of other private funds and aside from those assets substantially all of that fund's remaining assets are held in cash and cash equivalents and instruments acquired for the purpose of hedging currency exposure, the adviser is only required to complete Section 1b for that private fund.

D. Reporting for Affiliated and Sub-advised Funds

An adviser *may* report the private fund assets that it manages along with the private fund assets that its related persons manage on a single Form PF, but is not obligated to do so. Only one adviser to a sub-advised private fund should report information on Form PF with respect to that private fund. The same adviser that completes Form ADV with respect to that private fund is required to complete Form PF. If the adviser that completes Form ADV with respect to that private fund is not required to file Form PF (for instance, it is an exempt reporting adviser), then another registered adviser must report on behalf of that private fund.¹³

E. What Information Must Be Provided on Form PF?

Form PF consists of five sections. All private fund advisers required to file Form PF must complete Sections 1a ("Information about you and your related persons") and 1b ("Information about the private funds you advise"). Section 1a requires identifying information about the adviser and basic aggregate information about the types of private funds managed. An adviser generally must complete a separate Section 1b for each private fund advised, providing, among other items, information about its borrowings, its gross and net assets, the assets and liabilities of the private fund categorized into three levels based on the availability of pricing information,¹⁴ the gross aggregate notional value of derivative positions (with the value of options being reported using their delta adjusted notional value), the percentage of the private fund's equity owned by its five largest beneficial owners, and a breakdown of the beneficial ownership of the private fund by categories of investors. Section 1b also requires gross and net performance information for the fund, but that is based on performance as reported to current and prospective investors (or already calculated for other purposes) so that monthly and quarterly results are required only if they are so reported (or otherwise calculated). All hedge fund advisers are required to complete Section 1c ("Information about the hedge funds you advise"), which requests information such as each fund's investment strategy, the percentage of the fund's assets managed using a high-frequency trading strategy and any significant counterparty exposures. Large private fund advisers are required to submit more detailed information in Sections 2, 3 and 4, as applicable. Section 5 is to be completed by private fund advisers requesting a temporary hardship exemption.

¹² See *Id.* at 45.

¹³ See *Id.* at 49.

¹⁴ Private funds that use U.S. GAAP or another accounting standard that uses a fair value hierarchy similar to that established under U.S. GAAP can use those standards. See Form PF Release at 70.

a. Large Hedge Fund Advisers

Large hedge fund advisers must complete Section 2 of Form PF and report information regarding the market value of assets invested (on a short and long basis) in different types of securities and commodities, the duration of fixed income portfolio holdings, the turnover rate of the adviser's aggregate portfolios and a geographic breakdown of investments held by each hedge fund advised. In addition, an adviser to a hedge fund having a net asset value greater than \$500 million (a "qualifying hedge fund," as defined in the Glossary of Terms) is required to report, in Section 2b, certain information relating to that hedge fund's portfolio liquidity, holdings of unencumbered cash and concentration of positions. All information in Section 2b is reported on a *per fund* basis, not on an aggregate basis.

b. Large Liquidity Fund Advisers

In addition to Section 1 of Form PF, a large liquidity fund adviser is also required to complete Section 3 of Form PF. Section 3 of Form PF requires, among other things, information on the types of assets held by a liquidity fund, as well as certain information relevant to the risk profile of the liquidity fund and the extent to which the liquidity fund has a policy of complying with some or all aspects of the rules applicable to registered money market funds under the 1940 Act.

c. Large Private Equity Fund Advisers

In addition to Section 1 of Form PF, a large private equity fund adviser is also required to complete Section 4 of Form PF. Among other things, Section 4 requires various information about leverage at the controlled portfolio companies¹⁵ of each private equity fund overall, including information regarding debt-to-equity ratios, whether borrowings are current or long-term liabilities, the percentage that is PIK or zero-coupon, and whether the private fund or any of its controlled portfolio companies have experienced an event of default. No portfolio companies are required to be identified for this information, but the identities of counterparties to bridge financings (and the amount of their exposure) is to be provided. Information about the total value of guarantees by the private equity fund adviser and its affiliates of portfolio company obligations is also required. In addition, large private equity fund advisers are required to identify and provide certain information regarding their controlled portfolio companies that are banks or certain other financial companies. Finally, Section 4 requires a breakdown of each private equity fund's investments by industry and certain geographical categories and information about the amount of investments in portfolio companies by the adviser and its related persons.

¹⁵ Control, for this purpose, has the same definition as under Form ADV (which includes a presumption of control if there is the right to vote or direct the sale of 25% or more of a class of voting securities of a corporation) but also includes control by a club or consortium.

F. Confidentiality Concerns

The SEC is required to keep information submitted on Form PF confidential, although it may use and disclose such information in certain circumstances.¹⁶ With respect to the CFTC, the Dodd-Frank Wall Street Reform and Consumer Protection Act¹⁷ exempts the CFTC from being compelled under the Freedom of Information Act to disclose to the public any information collected through Form PF and requires that the CFTC maintain the confidentiality of that information consistent with the level of confidentiality established for the SEC in Section 204(b) of the Investment Advisers Act. Although the Dodd-Frank Act contemplates that the data may be shared with other Federal departments or agencies or self-regulatory organizations, such entities may use the information only for purposes within the scope of their jurisdiction.

Further, in an attempt to alleviate advisers' concerns with respect to position level disclosure, Form PF requires that an adviser identify only its exposure within broad asset classes, not its individual investment positions.¹⁸

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If you have any questions concerning the matters described in this memorandum, please contact Daniel Schloendorn (212-728-8265, dschloendorn@willkie.com); Rita M. Molesworth (212-728-8727, rmolesworth@willkie.com); Adrienne L. Atkinson (212-728-8253, aatkinson@willkie.com); James G. Silk (202-303-1275, jsilk@willkie.com); Martin R. Miller (212-728-8690, mmiller@willkie.com); Elizabeth G. Miller (212-728-8611, emiller@willkie.com); Vadim Avdeychik (202-303-1185, vavdeychik@willkie.com); or the Willkie attorney with whom you regularly work.

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¹⁶ See Section 204(b)(8) of the Investment Advisers Act.

¹⁷ The Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

¹⁸ See Form PF Release, *supra* note 1, at 113, n.343.