

CLIENT MEMORANDUM

U.S. House Expected to Pass Legislation Exempting Some Private Equity Advisers From SEC Registration and Reporting Rules

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As early as December 4 of this year, the U.S. House of Representatives is expected to vote on legislation that would exempt certain private equity fund advisers from U.S. Securities and Exchange Commission ("SEC") registration and reporting rules. The bill is expected to pass the House, but its prospects for a vote in the U.S. Senate and enactment into law are uncertain.

Background

Title IV of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") significantly changed the adviser registration requirements. As a result, many advisers to private investment funds, including private equity funds, must register with the SEC. The Dodd-Frank Act exempts a limited group of advisers from this registration requirement, including advisers to private funds with assets under management of less than \$150 million (subject to recordkeeping and reporting requirements); "family offices," as defined by the SEC; and advisers to certain venture capital funds. Such exemptions have generally proven to be unavailable to traditional private equity firms.

SEC adviser registration requirements trigger significant additional recordkeeping and reporting requirements. Registered advisers must complete SEC Form PF, under which advisers to private equity funds must report assets under

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management of each fund, use of leverage at the fund and portfolio level, certain counterparty credit exposure, geographical and industry distribution of investments, ownership by categories of investors, fund performance and other information. The SEC shares this information with the Financial Stability Oversight Council ("FSOC") and other regulators.

The SEC requirements have prompted concerns from advisers and members of Congress that the requirements are costly and, that while perhaps appropriate with regard to certain advisers, are disproportionately burdensome to private equity advisers in light of their arguably marginal benefit with respect to private equity investors.

H.R. 1105: The Small Business and Capital Access and Job Preservation Act

H.R. 1105, introduced by Rep. Robert Hurt (R-VA), has 12 cosponsors: seven Democrats and five Republicans. According to the House Committee on Financial Services report on the bill, H.R. 1105 "exempts advisers to private equity funds that have not borrowed and that do not have outstanding a principal amount in excess of twice their funded capital commitments."

The bill further requires the SEC, within six months of enactment, to issue rules defining the term "private equity fund" and requiring exempted advisers to maintain records and provide reports that the SEC determines are "necessary and appropriate in the public interest and for the protection of investors." In establishing the latter rule, the SEC is to take into account "fund size, governance, investment strategy, risk and other factors."

Prospects for H.R. 1105

H.R. 1105 is expected to pass the House with a bipartisan majority. However, when the bill was taken up by the House Committee on Financial Services, the vote to report it to the full House was 38 in favor and 18 against, with most opposition coming from Democratic Committee members. As a result, it is likely that there will be a substantial number of "no" votes in the full House.

The House Committee on Financial Services report on the bill includes minority views signed by 11 Democratic members of the Committee, including the senior Democratic member, Rep. Maxine Waters (D-CA). They acknowledge that, while there may be room for improvement in the adviser registration requirements, those requirements have been in effect for over a year, and have benefits that outweigh their costs and burdens. They note that registered advisers must "provide advice that is in the best interest of the investor," set up compliance programs and codes of ethics, and name compliance officers. They describe the reports advisers file as including "basic disclosures about an employee who violated securities laws, the adviser's business practices, its fees, and any conflicts of interest."

The dissenting members also predict that the leverage standard in the bill will result in exempting "all" private equity funds. Finally, they object to the easing of adviser registration and reporting requirements just as the SEC is about to permit

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private equity and other private funds to advertise and make general solicitations under the Jumpstart Our Business Startups Act of 2012 ("JOBS Act").

These objections, which are being echoed by some public interest groups, indicate that opposition to the bill is significant. Assuming the House passes the bill, its prospects in the Senate are uncertain. Senate Democratic leadership may be reluctant or unwilling to bring up the bill for a Senate vote. Some, and possibly many, Democratic senators may share the views of House and public interest group opponents. In addition, Senate Democrats have been unwilling to consider any legislation that would change specific provisions of the Dodd-Frank Act because under Senate rules such legislation would risk opening the entire law to proposed amendments. Finally, the Obama Administration has announced that the President's advisers would recommend that the bill be vetoed if it reaches the President's desk.

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