

# Alerts & Publications

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## Reporting Under Dodd-Frank: Disclosure of Extensive Information Regarding Private Funds Managed by Private Fund Advisers

February 7, 2011

Pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (“Dodd-Frank Act”), the Securities and Exchange Commission (“SEC”) and the Commodity Futures Trading Commission (“CFTC,” and together with the SEC, the “Commissions”) jointly issued a rule proposal (“Release”)<sup>1</sup> that would require certain investment advisers to private funds (“Private Fund Advisers”) to periodically report detailed information about such funds to assist the Financial Stability Oversight Council (“FSOC”) in monitoring and assessing systemic risk to the U.S. financial system.<sup>2</sup> The Release proposes new Rule 204(b)-1 under the Investment Advisers Act of 1940, as amended (“Advisers Act”), requiring Private Fund Advisers to electronically file Form PF to report information about the private funds they advise, including the types and amounts of investments made by the funds, the funds’ assets and borrowings, the funds’ ownership structure, and performance information. Such information will be used by the FSOC to determine which Private Fund Advisers should be supervised by the Board of Governors of the Federal Reserve System (“FRB”), in addition to oversight by the SEC. In addition, the FSOC may direct the U.S. Department of the Treasury’s Office of Financial Research to collect additional information from Private Fund Advisers as it deems necessary.

### **Private Fund Advisers Required to File Form PF**

The proposed rule would require many advisers to private funds to disclose a significant amount of information about the funds they manage. The Release defines “Private Fund Advisers” as investment advisers that (i) are registered or required to register with the SEC (including any investment adviser that is also registered or required to register with the CFTC as a CPO or CTA), and (ii) advise one or more “private funds.”<sup>3</sup> The broad definition of “private funds” would include structured finance vehicles and structured products, such as collateralized loan obligations and collateralized debt obligations, in addition to other investment funds.

### *Large Private Fund Advisers*

The Release identifies the following three types of “Large Private Fund Advisers” that would be required to provide significantly more detailed information on Form PF:

- Advisers managing hedge funds that collectively have at least US\$1 billion in assets as of the close of business on any day during a reporting period (“Large Hedge Fund

Advisers”);<sup>4</sup>

- Advisers managing a liquidity fund and having combined liquidity fund and registered money market fund assets of at least US\$1 billion as of the close of business on any day during a reporting period (“Large Liquidity Fund Advisers”);<sup>5</sup> and
- Advisers managing private equity funds that collectively have at least US\$1 billion in assets as of the close of business on the last day of the quarterly reporting period for the required report (“Large Private Equity Fund Advisers”).<sup>6</sup>

Private Fund Advisers would be required to measure on a *daily* basis whether the US\$1 billion thresholds have been crossed for hedge funds and liquidity funds, which could present advisers with significant challenges. For private equity funds, advisers would have to measure whether the US\$1 billion threshold has been crossed on a quarterly basis.

Under the Release, each of the Large Private Fund Advisers would be required to complete a different section of the Form PF.

#### *Aggregation of Assets*

In order to determine whether an adviser is a Large Private Fund Adviser, each adviser would have to aggregate (i) the assets of “parallel managed accounts” (i.e., managed accounts or other pools of assets advised by the adviser that pursue substantially the same investment objective and strategy and invest in substantially the same positions as the private fund) and (ii) assets of that type of private fund advised by any of the adviser’s “related persons” (e.g., affiliates that are under common control with the Private Equity Fund Adviser).

#### *Exempt Advisers*

Advisers to venture capital funds and advisers solely to private funds that have less than US\$150 million in assets under management in the United States (collectively, “exempt reporting advisers”) would not be required to file Form PF. Under the Dodd-Frank Act, such exempt reporting advisers are not required to register under the Advisers Act, but would be required to comply with record-keeping and SEC examination requirements imposed by the Dodd-Frank Act. In addition, “foreign private advisers” (as defined in Section 402 of the Dodd-Frank Act), which are exempt from registering under the Advisers Act and from record-keeping and SEC examination requirements, also would not be required to file Form PF.<sup>7</sup>

#### **Form PF Filing Requirements**

Form PF is separated into four sections, and Private Fund Advisers are required to complete specific sections of the form, based on their size and type. Large Private Fund Advisers would be required to file the Form PF on a quarterly basis within 15 days of the quarter end, which could pose serious challenges in terms of compiling the necessary information in order to timely submit the Form PF, while all other Private Fund Advisers would be required to file annually.

Much of the information requested by Form PF is confidential, and the Release provides that the information will be kept confidential, and may only be shared with the FSOC and certain bodies of the federal government and self-regulatory organizations in the manner set forth in Section 404 of the Dodd-Frank Act. As provided in Section 404 of the Dodd-Frank Act, the information disclosed on Form PF would not be subject to Freedom of Information Act requests. The SEC may, however, share information reported on Form PF with foreign financial regulators under information sharing agreements where the foreign regulator agrees to keep the information confidential.

#### *Section 1: All Private Fund Advisers*

Section 1 would be required to be completed by all Private Fund Advisers and would require disclosure of the following, in addition to other information:

- Total “regulatory assets under management”<sup>8</sup>
- Net assets under management
- Each private fund’s gross and net assets
- The aggregate notional value of each fund’s derivative positions
- Monthly and quarterly performance information for each fund
- Information about each fund’s borrowings, including the identity of, and amount owed to, each creditor to which the fund owed an amount equal to or greater than 5% of the fund’s net asset value (“NAV”)

As proposed, Form PF would also require disclosure of information about each hedge fund managed by the Private Fund Adviser, if any, including the following information:

- The hedge fund’s investment strategies and percentage of NAV represented by the strategy
- The percentage of the hedge fund’s NAV that are managed using computer-driven trading algorithms to select investments
- Trading and clearing practices
- The identity of the five trading counterparties to which the hedge fund have the greatest net counterparty credit exposure, and that have the greatest net counterparty credit exposure to the fund

### *Section 2: Large Hedge Fund Advisers*

Section 2 of Form PF would require Large Hedge Fund Advisers to disclose information about the hedge funds they manage, including by way of example:

- The market value of hedge fund assets invested in different types of securities products (e.g., listed and unlisted equity, bonds, loans, commodities and other derivatives, etc.) to include both long and short positions
- The turnover rate of their aggregate portfolios of the hedge funds they advise
- A geographic breakdown of the investments held by the hedge funds

In addition, for each “qualifying hedge fund” (i.e., a hedge fund with a net asset value of at least US\$500 million as of the close of business on any day during the reporting period) managed by a Large Hedge Fund Adviser, Form PF would require the disclosure of additional information, including the following:

- The market value of assets invested in different types of securities products (both long and short positions)
- Information regarding the qualifying hedge fund’s portfolio liquidity and concentration
- Collateral practices with the top five counterparties identified in Section 1 of Form PF (and discussed above)
- The identity of, and clearing relationships with, the three central clearing counterparties to which the fund has the greatest net counterparty credit exposure
- Hedge fund risk metrics, including the impact of market factors and the monthly value at risk (“VaR”) metric, if the Large Hedge Fund Adviser regularly calculated VaR during the quarter
- Financing information, including a monthly breakdown of its secured and unsecured borrowing from various types of creditors and its derivatives exposures
- The fund’s investor composition and liquidity, including whether the fund uses side pocket arrangements or imposes gating restrictions on investor withdrawals and redemptions

### *Section 3: Large Liquidity Fund Advisers*

Section 3 of Form PF would require Large Liquidity Fund Advisers to report certain information for each liquidity fund they manage, including, by way of example, the following:

- The fund’s assets, including the gross dollar value of the fund’s open positions in specific asset classes along with maturity information for each instrument
- Secured and unsecured borrowing, including creditor type and the latest date the principal can be repaid without defaulting or incurring additional fees, but only if the total amount borrowed by the liquidity fund represents 5% or more of the fund’s NAV

- A good faith estimate of the percentage of the liquidity fund purchased using securities lending collateral
- The fund's investor composition and liquidity, including gating restrictions on withdrawals and redemptions

#### *Section 4: Large Private Equity Fund Advisers*

Section 4 of Form PF would require Large Private Equity Fund Advisers to report certain information about financing and investments for each private equity fund they advise, including by way of example:

- Whether any fund guarantees the obligations of any of its portfolio companies
- Information related to financing practices, including the maturity profile of debt held by portfolio companies controlled by the private equity fund
- The fund's investments by industry and geographic location
- Whether any related persons co-invest in any of the private equity fund's portfolio companies, along with the aggregate dollar amount of such investments.

#### **Reporting for Affiliated and Sub-Advised Funds**

Private Fund Advisers with related persons that would also be required to file Form PF may report a single Form PF for all related persons and the private funds they advise, however, filing a single Form PF is not required of affiliated Private Fund Advisers. With respect to sub-advised funds, the Release provides that only one Private Fund Adviser should file Form PF for such sub-advised fund in order to prevent duplicative reporting. If a Private Fund Adviser completes Section 7.B.1 of Part I of Form ADV with respect to any private fund, such adviser would be responsible for filing Form PF with respect to that fund.<sup>9</sup>

#### **Effective Date**

The Release anticipates that the new rule requiring the filing of Form PF would have a compliance date of December 15, 2011, meaning that Large Private Fund Advisers would have to make their initial Form PF filing by January 15, 2012, and then quarterly thereafter. All other Private Fund Advisers would have 90 days after the end of their first fiscal year following the December 15, 2011 compliance date to file their first Form PF (e.g., Private Fund Advisers with a December 31 fiscal year end would have to file their first Form PF by March 31, 2012).

1. Reporting by Investment Advisers to Private Funds and Certain Commodity Pool Operators and Commodity Trading Advisors on Form PF, Release No. IA-3145 (Jan. 26, 2011), available at <http://www.sec.gov/rules/proposed/2011/ia-3145.pdf>.

2. The Release would also require commodity pool operators ("CPO") and commodity trading advisers ("CTA") registered with the CFTC to fulfill certain filing requirements. This client alert does not address filing requirements proposed for CFTC-registered organizations.

3. The Dodd-Frank Act defines a "private fund" as a fund that would be an investment company under the Investment Company Act of 1940, as amended (the "Investment Company Act") but for the exceptions in Section 3(c)(1) or Section 3(c)(7) of the Investment Company Act.

4. As proposed, Form PF defines "hedge fund" as any private fund that (1) has a performance fee or allocation calculated by taking into account unrealized gains; (2) 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 (3) may sell securities or other assets short.

5. A "liquidity fund" would be 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.

6. A “private equity fund” would be any private fund that is not a hedge fund, liquidity fund, real estate fund (i.e., any private fund that is not a hedge fund, that does not provide investors with redemption rights in the ordinary course and that invests primarily in real estate and real estate-related assets), securitized asset fund (i.e., any private fund that is not a hedge fund and that issues asset backed securities and whose investors are primarily debt-holders) or venture capital fund and does not provide investors with redemption rights in the ordinary course.

7. See link for a discussion of exempt reporting advisers and foreign private advisers.

8. “Regulatory assets under management” should be calculated in accordance with the definition set forth in Instruction 5.b in proposed amendments to Part 1 of Form ADV. See Rules Implementing Amendments to the Investment Advisers Act of 1940, Release No. IA-3110 (Nov. 19, 2010), available at <http://sec.gov/rules/proposed/2010/ia-3110.pdf> [hereinafter *Form ADV Amendments*]. The Release notes that the regulatory assets under management reported on Form ADV may differ from the amount to be reported on Form PF for advisers (i) that file Form PF quarterly, or (ii) that advise parallel managed accounts that are not “securities portfolios” as defined in Instruction 5.b of Form ADV.

9. See *Form ADV Amendments*.