

Recent SEC Developments Affecting Hedge Funds

Please note the following recent SEC developments affecting hedge funds:

“Accredited Investor” Definition

At an open meeting on December 13, 2006, the SEC voted to propose a change to the definition of “accredited investor” that, if adopted, would apply to offers and sales of securities issued by hedge funds and other private investment pools to natural persons. The proposal requires individuals to be both “accredited investors” under the existing standards and own not less than \$2.5 million in investments (as currently defined in the Investment Company Act for purposes of the Section 3(c)(7) exemption) on the date an investment is made. The \$2.5 million test will be periodically adjusted for inflation.

The staff of the SEC noted that the new definition would not apply to individual investors in venture capital funds, but did not offer any additional information about whether any other types of funds would be excluded.

Advisers Act Anti-Fraud Provision

At the December 13 open meeting, the SEC also voted to propose a rule that would provide that an investment adviser would violate Section 206(4) of the Investment Advisers Act of 1940 if it makes materially false or misleading statements to investors or prospective investors in an investment pool. The rule would apply both to investment advisers who are registered under the Advisers Act and to unregistered advisers.

The SEC has not yet made available the text of either of the proposed rules, so many details are still uncertain. We will keep you apprised of any updates.

Changes to Short Sale Rules

On December 6, 2006, the SEC proposed amending Rule 105 under Regulation M to provide that it is unlawful to effect a short sale in a security within five business days prior to pricing of a public offering of such security (or during the period beginning with the filing of the registration statement and ending with pricing, if that period is shorter than five business days) and then to purchase such security in the offering. Under the current version of Rule 105, it is only unlawful to cover a short sale entered into within five business days prior to pricing with securities purchased in the offering; purchases in the offering are permitted as long as the shares purchased are not used to cover the short sale.

On December 7, 2006, the SEC proposed to eliminate Rule 10a-1 under the Securities Exchange Act of 1934 (the “uptick rule”), and to adopt a rule which would provide that no short sale price test (including any test established by any self-regulatory organization) may apply with respect to short sales in any security.

Comments on both rules should be provided on or before February 12, 2007. The text of the SEC releases describing the proposed rules are available at <http://www.sec.gov/rules/proposed/2006/34-54888.pdf> (the amendment to Rule 105) and <http://www.sec.gov/rules/proposed/2006/34-54891.pdf> (the elimination of short sale price tests).

Contact Information

If you have any questions or would like to learn more about any of these developments, please contact your usual legal advisor at Ropes & Gray LLP.

