ROPES & GRAY

Preparing for Financial Reform: Investment Adviser Registration

On May 20, 2010, the U.S. Senate passed *The Restoring American Financial Stability Act of 2010* (the Senate bill), which proposes to restructure the U.S. financial regulatory system by providing for more extensive regulation of banks and other large financial institutions, over-the-counter derivative markets, consumer financial products and services, investment advisers, short sales, credit rating agencies, and mortgage lending. In December 2009, the U.S. House of Representatives passed its own version of comprehensive financial regulatory reform entitled *The Wall Street Reform and Consumer Protection Act of 2009* (the House bill) for an analysis of the House bill click here. Differences between the Senate and House bills must be reconciled by conference committee and approved by Congress before the President can sign financial reform legislation into law. Congressional leaders are reportedly seeking to submit a final piece legislation to President Obama before July 4th.

Registration and Reporting Requirements Under the Advisers Act

Like the House bill, the Senate bill would substantially alter the registration and reporting schemes under the Investment Advisers Act of 1940 (the Advisers Act). Most notably, both bills would require all U.S. hedge fund advisers (and most non-U.S. advisers to hedge funds with U.S. investors) above a modest asset-under-management threshold to register with the SEC as investment advisers under the Advisers Act. The House bill, unlike the Senate bill, would also extend this requirement to private equity fund advisers. The key similarities and differences between the investment adviser registration and reporting provisions of the two bills are as follows:

Key similarities between the Senate bill and the House bill:

- The elimination of the so-called "private adviser exemption" from registration in Section 203(b)(3) of the Advisers Act, which currently exempts investment advisers that do not hold themselves out to the public as investment advisers and have fewer than 15 clients.
- An exemption from registration for investment advisers with respect to the provision of investment advice to "venture capital funds" (the definition of a venture capital fund to be determined by the Securities and Exchange Commission (the SEC)).
- An exemption from registration for "foreign private advisers" (*i.e.*, an investment adviser that: (i) has no place of business in the United States; (ii) has fewer than 15 U.S. clients; (iii) has less than $25 million in assets under management attributable to U.S. clients; and (iv) does not hold itself out to U.S. investors as an investment adviser).
- Enhanced reporting requirements for registered investment advisers to private funds, including disclosing the amount of assets under management, counterparty credit risk exposure and trading and investment positions.
- An exemption from registration for investment advisers to small business investment companies licensed under the Small Business Investment Act of 1958.
- An effective date for the changes to existing registration and reporting requirements of one year from the date the legislation is enacted into law.

Key differences between the Senate bill and the House bill:

- The Senate bill provides for an exemption from registration for investment advisers with respect to the provision of investment advice to "private equity funds" (the definition of a private equity fund to be determined by the SEC).
- The Senate bill directs the SEC to issue rules to require investment advisers to private equity funds that are exempt from registration to maintain such records and provide the SEC such annual or other reports as the SEC determines is necessary. The House bill provides for a similar requirement, but only as it relates to investment advisers to venture capital funds that are exempt from registration.
- The Senate bill provides for an exemption from registration for investment advisers with less than $100 million of assets under management that are subject to regulation by the state in which such investment adviser maintains its principal place of business. The House bill directs the SEC to provide an exemption for investment advisers to private funds that have assets under management in the United States of less than $150 million and to issue rules to require such investment advisers to maintain such records and provide the SEC such annual or other reports as the SEC determines is necessary.
- The House bill eliminates the existing exemption from registration for investment advisers of private funds that are registered with the Commodity Futures Trading Commission.

The Senate bill also directs the SEC to amend the net worth threshold for "accredited investor" status under the Securities Act of 1933 for natural persons (including joint net worth with spouse) to at least $1 million, excluding the value of such individual's primary residence (under current law, a natural person may include the value of such person's primary residence in determining his or her net worth).

Upon passage of final financial regulatory reform legislation, Ropes & Gray will issue another alert describing in more detail the impact of the legislation on investment advisers. In the meantime, if you have any questions about the Senate bill or the House bill, please contact the Ropes & Gray attorney who normally advises you or one of the attorneys from the above-listed Ropes & Gray practices.

We are monitoring the progress of financial reform legislation, especially those changes that may affect the investment management, banking, hedge and private investment fund, and derivatives businesses. If you have questions concerning **Financial Reform Matters**, please contact any of the attorneys listed below or the Ropes &Gray attorneys with whom you regularly work.

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