May 11, 2023

Analysis of Amendments to Form PF

The SEC adopted amendments to Form PF (the "Amendments") on May 3, 2023. The Amendments include (i) new current reporting requirements for large hedge fund advisers; (ii) new quarterly and annual event reporting for advisers to private equity funds; and (iii) amendments to certain annual reporting requirements for large private equity fund advisers.

The Amendments will become effective (i) six months after the publication of the adopting release in the Federal Register (which can take several weeks) for the event reporting requirements noted below, and (ii) one year after publication in the Federal Register for the remainder of the requirements. The full adopting release (the "Adopting Release") is available here: https://www.sec.gov/rules/final/2023/ia-6297.pdf

The SEC did not adopt proposed changes to Form PF designed to align large liquidity fund adviser reporting with amendments that the SEC separately proposed to Form N-MFP for money market funds, as the proposed changes to Form N-MFP are still under consideration. In August 2022, the SEC and the CFTC jointly proposed amendments to Form PF to expand reporting requirements for all filers regarding fund structures and investments, including new requirements for large hedge fund advisers to report on certain digital asset investments. That joint proposal remains under consideration by the SEC and the CFTC, and the Amendments do not address those proposed changes.

New Current Reporting for Large Hedge Fund Advisers

The Amendments include new requirements for large hedge fund advisers (hedge fund advisers with at least $1.5 billion in hedge fund AUM) to file current reports within 72 hours of the occurrence of certain reporting events. Large hedge fund advisers will be required to provide the current reports through the Private Fund Reporting Depository (PFRD) on newly created Section 5 of Form PF. To the extent reporting is required, the adviser will only file Section 5 and will not submit any other sections of Form PF.

Timing and Amendments. The reports must be submitted as soon as practicable, but no later than 72 hours from the occurrence of a reportable event. This is a change from the proposal, which contemplated reporting within one business day. The reporting period begins at the time of the event, or the time when the adviser reasonably believes the event occurred. For example, if a reportable event occurred at noon on Thursday, the report would be required to be filed by Sunday before noon. The adviser must respond to the best of its knowledge as of the date of the report and is permitted to file an amendment to correct information that was inaccurate or filed in error.

Reportable Events. Section 5 requires reporting with respect to certain reportable events as described below.

Extraordinary Investment Losses. Item B of Section 5 requires reporting of extraordinary investment losses, which are defined as losses equal to or greater than 20% of the "reporting fund aggregate calculated value" ("RFACV"), rather than the fund's most recent net asset value (as originally proposed), over a period of 10 business days. For example, an adviser would be required to file a report where the fund's RFACV is $1 billion and the fund loses $20 million per business day for 10 consecutive business days. Because the 10-business-day period is backward-looking, the adviser would also be required to report a loss of $200 million in one business day.

RFACV is calculated as "every position in the reporting fund's portfolio, including cash and cash equivalents, short positions, and any fund-level borrowing, with the most recent price or value applied to the position for purposes of managing the investment portfolio." The SEC clarified that RFACV is calculated on a net basis rather than gross (and therefore liabilities would be subtracted). It is not necessary to adjust the RFACV for accrued fees or expenses. The Adopting Release also notes that RFACV is intended to be compiled on a best-efforts basis and calculated in a manner similar to daily profit and loss. The SEC noted the calculation should "generally include all items at their most recent,

reasonable estimate, which will be marked-to-market for all holdings that can reasonably be marked daily." Advisers are permitted to calculate RFACV using their own methodologies (or those of their service providers), provided they are consistent with the adviser's internal reporting.

If the trigger occurs, an adviser must report (i) the beginning and ending date of the 10-business-day period, (ii) the holding period return, and (iii) the dollar amount of loss over the period. In order to calculate the rate of return for the 10-business-day holding period, the Amendments add new definitions to the Form PF Glossary for "holding period return" and "daily rate of return."

To the extent that losses continue past the initial 10-business-day period, subsequent reporting is not required until on or after the fund has lost an additional 20% over a second 10-business-day period, beginning on or after the end date of the original reporting event.

Margin, Collateral or Equivalent Increase. Item C of Section 5 requires advisers to report an increase in the total dollar value of a reporting fund's requirements for margin, collateral or an equivalent of 20% or more within a rolling 10-business-day period. In another change from the proposal, the SEC ultimately determined not to calculate the 20% based on the fund's most recent net asset value, as was originally proposed. The 20% reporting threshold is calculated based on "average daily reporting fund aggregate calculated value," a new defined term in the Form PF glossary, which represents the average of the daily RFACV as of the end of each business day in the 10-business-day reporting period. The Adopting Release explains that margin, collateral or an equivalent is intended to refer to assets and cash that can be claimed by a fund counterparty, lender, or clearinghouse if needed to satisfy an obligation, whether they have been physically segregated or marked and identified as collateral.

If the trigger occurs, an adviser must report (i) the beginning and ending date of the 10-business-day period (ii) the total dollar value amount of margin, collateral or equivalent posted by the reporting fund at the beginning and ending dates of the 10-business-day period; (iii) the average daily reporting fund aggregate calculated value during the 10-business-day period; and (iv) the identity of the counterparty or counterparties that required the increase. Item C also requires the adviser to report its current understanding of the circumstances relating to the increase and provides check boxes for the following scenarios: (i) exchange or central clearing party requirements or known regulatory action affecting one or more counterparties; (ii) one or more counterparties independently increased the margin requirements; (iii) the reporting fund established a new relationship or new business with one or more counterparties; (iv) new investment positions, investment approach or strategy and/or portfolio turnover; (v) a deteriorating position or positions in the portfolio or other credit trigger under applicable counterparty agreements; and/or (vi) a reason other than those outlined, which requires the adviser to provide an explanatory note.

To the extent margin increases continue past the initial 10-business-day period, subsequent reporting is not required until the next 10-business-day period beginning on or after the end date in the initial Item C report and only if there is a subsequent increase of 20% or more.

Fund Margin Default or Inability to Meet Margin Call. Item D of Section 5 requires reporting in the event of a fund's margin default or inability to meet a call for margin, collateral or an equivalent, taking into account any contractually agreed cure period. Reporting is required where there is a dispute regarding the margin call; however, advisers are not required to report where there is a dispute as to the amount and appropriateness of the margin call, provided that the reporting fund has sufficient assets to meet the greatest of the disputed amount.

If the trigger occurs, an adviser must report, with respect to each counterparty for which a margin event occurred, (i) the date that the adviser determines or is notified that the reporting fund is in margin default or is unable to meet a margin call; (ii) the dollar amount; and (iii) the legal name and LEI of the counterparty. The adviser is also required to select from the following check boxes to explain its current understanding of why the margin event occurred: (i) a

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counterparty's increase in margin requirements; (ii) portfolio losses or other credit trigger under the applicable counterparty agreement; (iii) a default or settlement failure of a counterparty; or (iv) a reason other than those outlined, in which case the adviser is required to provide an explanatory note.

Counterparty Default. Item E of Section 5 requires advisers to report a counterparty's margin, collateral or equivalent default or failure to make other payment in the time and form contractually required (taking into account any contractually agreed cure period) where the amount involved is greater than 5% of the RFACV.

If the trigger occurs, an adviser must report (i) the date of the default; (ii) the dollar amount of the default; and (iii) the legal name and LEI of the counterparty.

Termination or Material Restriction of Prime Broker Relationship. The SEC originally proposed to require advisers to report any material change in the relationship between the reporting fund and a prime broker. Item E as adopted requires an adviser to file a report when (i) a prime broker terminates or materially restricts its relationship with the reporting fund, in whole or in part, in markets where the prime broker continues to be active; or (ii) the relationship between the prime broker and the reporting fund is terminated by either party, and a termination event was activated in the prime brokerage agreement within the last 12 months. With respect to terminations or material restrictions by the prime broker, if a prime broker ceases operations in a particular market for all clients, no report is required; however, if the prime broker will no longer conduct certain trades on behalf of a reporting fund in a particular market, the adviser would be required to report that material restriction. A material restriction also includes scenarios where a prime broker introduces substantial changes to credit limits or significant price increases, ceases to support a particular fund in an important market or asset type, or otherwise significantly limits a fund's ability to operate under the terms of the original agreement or impairs the fund's ability to trade. With respect to terminations by either party, the instructions to Item E clarify that reporting is not required if the termination event relates solely to the financial state, activities, or other conditions relating only to the prime broker. Also, a termination due to non-renewal at the end of the contract term does not need to be reported.

If a trigger occurs, an adviser must report (i) the date of the termination or material restriction; (ii) the date of the termination event, if different; and (iii) the legal name and LEI of the prime broker.

Operations Events. Item G of Section 5 requires reporting with respect to any "significant disruption or degradation" of the reporting fund's "critical operations." Under the original proposal, a "significant disruption or degradation" would have been defined to include a 20% threshold (i.e., any disruption that resulted in a 20% disruption or degradation of normal volume or capacity). The SEC determined not to include a definition of "significant disruption or degradation" in the Amendments, although the Adopting Release notes that a 20% threshold may be generally indicative of an event that should be reported. Critical operations are operations necessary for (i) the investment, trading, valuation, reporting, and risk management of the reporting fund, or (ii) the operation of the reporting fund in accordance with the Federal securities laws and regulations. The Adopting Release does not further elucidate these critical operations, except to provide the example that a reporting obligation would arise if certain key persons integral to a fund's operations, trading systems, or software are unavailable, and the adviser or fund is therefore unable to perform critical operations.

If a trigger occurs, an adviser must report: (i) the date the event occurred (or an estimate); (ii) the date the event was discovered; and (iii) whether the adviser has initiated a disaster recovery or business continuity plan relating to the event. Item G also requires the adviser to select from check boxes to provide its current understanding of the circumstances that led to the event, which include (i) the event occurred at a service provider (and specify which service provider); (ii) the event occurred at a reporting fund or adviser or a related person; (iii) the event is related to a natural disaster or other force majeure event; or (iv) other (which requires an explanatory note). The form also requires the adviser to select from check boxes to report its current understanding of the impact of the event on normal operations, including whether the event resulted in disruption or degradation of: (i) trading of portfolio assets; (ii) valuation of portfolio assets; (iii) the

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management of the reporting fund's investment risk; (iv) the ability to comply with applicable laws, rules, and regulations; or (v) other (which requires an explanatory note).

Large Withdrawal and Redemption Requests, Inability to Satisfy Redemptions, or Suspension of Redemptions. Item H of Section 5 requires an adviser to report the receipt of cumulative requests for withdrawals or redemptions from the reporting fund equal to or more than 50% of the most recent net asset value (after netting against subscriptions or other contributions from investors received and contractually committed). The reporting obligation does not take into account any pre-existing gates or limitations that might lower the percentage of net asset value actually subject to a redemption request. Item H requires the adviser to report: (i) the date on which the net redemption requests reached or exceeded 50% of the most recent net asset value; (ii) the net value of redemptions paid from the reporting fund between the last data reporting date (the end of the most recently reported fiscal quarter on Form PF) and the date of the current report; (iii) the percentage of the fund's net asset value the redemption requests represent; and (iv) whether the adviser has notified investors that the reporting fund will liquidate. To the extent that the adviser believes the large withdrawals are occurring in the ordinary course of business for the fund, the adviser can include an explanatory note to that effect.

If a trigger occurs, an adviser must report if a reporting fund (i) is unable to pay redemption requests, or (ii) has suspended redemptions and the suspension lasts for more than 5 consecutive business days. Item I requires the adviser to report: (i) the date the reporting fund was unable to pay redemption requests or suspended redemptions; (ii) the percentage of redemptions requested and not yet paid; and (iii) whether the adviser has notified investors that the reporting fund will liquidate.

Unencumbered Cash. The SEC did not adopt the proposed reporting requirements with respect to changes in unencumbered cash.

Observations.

- Large hedge fund advisors will need to implement monitoring systems to determine whether a reportable event has occurred and introduce new calculations (most notably, RFACV) in order to monitor reporting thresholds. While certain of these new tests can likely be added to the adviser's current monitoring software, others will require separate monitoring procedures. As a result, well in advance of the 6-month effective date, advisers will want to start modifying and creating monitoring procedures in the near term.
    - In practice, we expect the calculation for RFACV to be similar to NAV but without adjustments for accrued fees and expenses and without the requirement to conduct fair valuation procedures.
- The new margin, collateral or equivalent increase reporting item (Item C) defines a margin increase to include all assets and cash marked as collateral, which captures a hedge fund's entire prime brokerage account(s). Accordingly, this new item requires advisers to report, within 72 hours, any increase of 20% or more of a hedge fund's prime brokerage account balances over a rolling 10-day period, even if that increase is due to performance of the assets in the accounts.
- A number of the new reporting obligations require advisers to make subjective determinations, including with respect to whether there has been a "material restriction" with respect to a prime brokerage relationship, whether a "significant disruption or degradation" has occurred, and the scope of "critical operations." Advisers will need to develop procedures for identifying when a determination must be made as well as how to make these determinations.

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  - With respect to potentially reportable operational events, advisers will have to make sensitive judgments regarding material service providers. This may create complications to the extent different advisers make different reporting determinations with respect to the same service provider issue.

- For certain events, the 72-hour reporting deadline may be shorter than the originally proposed one business day. A reporting deadline may ultimately fall on a weekend or holiday.

New Quarterly Event Reporting for All Advisers to Private Equity Funds

The Amendments include new requirements for all advisers to private equity funds (advisers with at least $150 million in private equity fund AUM) to file quarterly reports with respect to certain reporting events. Reporting is required through PFRD on newly created Section 6 of Form PF. To the extent reporting is required, the adviser will only file Section 6 and will not submit any other sections of Form PF.

Timing. While the SEC originally proposed current reporting within one business day for advisers to private equity funds, the Amendments instead provide that new Section 6 of Form PF must be filed on a quarterly basis (and cited the Ropes & Gray comment letter in extending the time period for filing). In another departure from the proposal, and also in direct response to our comment letter, the SEC also moved reporting regarding clawbacks from an event reporting item to a new annual reporting item on Section 4. Accordingly, that reporting item (discussed in more detail in the annual reporting section further below) will only apply to large private equity fund advisers as part of their ordinary annual filing.

Section 6 must be filed within 60 days of the end of the reporting fund's fiscal quarter. Reporting is only required to the extent a reportable event occurred during the preceding quarter. Advisers are not required to report the same instance of a reporting event in subsequent filings. Accordingly, an adviser would only be required to file Section 6 once per reportable event.

Reportable Events.

Adviser-Led Secondary Transactions. Item B of Section 6 requires an adviser to provide reporting upon completion of an adviser-led secondary transaction. The Amendments define "adviser-led secondary transaction" to mean any transaction initiated by the adviser or any of its related persons that offers private fund investors the choice to: (i) sell all or a portion of their interests in the private fund or (ii) convert or exchange all or a portion of their interests in the private fund for interests in another vehicle advised by the adviser or any of its related persons. The Adopting Release clarifies that, while it is a facts and circumstances determination whether a transaction is "adviser-led," the adviser's or a related party's participation in a sale initiated by an unsolicited request of an investor generally would not be within scope. Item B requires the adviser to report the closing date of the transaction and a description of the transaction.

Removal of General Partner or Election to Terminate the Investment Period or Fund. Item C of Section 6 requires reporting upon receipt of notification that a fund's investors have: (i) removed the adviser or an affiliate as the general partner or similar control person of the fund; (ii) elected to terminate the reporting fund's investment period; or (iii) elected to terminate the fund under the fund's governing documents. This reporting requirement is limited to circumstances where action is taken by fund investors (i.e., reporting is not required for all terminations of a fund's investment period or of a fund). Item C requires reporting of the effective date and a description of the removal event.

General. Item D of Section 6 provides space for advisers to include an optional narrative response with respect to reportable events.

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Observations.

- Advisers will need to implement procedures to monitor whether a reportable event has occurred and ensure timely reporting. As a second layer, we believe it would be prudent for CCOs to consider, as part of their regular quarterly reviews, whether any event has occurred that would require reporting.
- Advisers are required to include a narrative description of the reportable event; however, the SEC did not discuss the extent or detail expected in response to these prompts. We expect advisers to use pre-drafted disclosure (e.g., a summary from continuation fund documents) to the extent possible in responding to the required narrative fields.
- Although the new reporting will require some additional resources, the result could have been more onerous, as the SEC ultimately adopted fewer quarterly reportable event triggers, and the timing will allow for quarterly reviews rather than requiring continuous monitoring and current reporting.

Amendments to Annual Reporting Items for Large Private Equity Fund Advisers

The Amendments also include new annual reporting items and amendments to certain existing reporting items for large private equity fund advisers (private equity fund advisers with at least $2 billion in private equity AUM) on Section 4 of Form PF. In a departure from the proposal, the SEC declined to lower the reporting threshold for large private equity fund advisers to $1.5 billion. The SEC also determined not to adopt proposed reporting items with respect to: (i) restructuring/recapitalization of a portfolio company; (ii) investments in different levels of a portfolio company's capital structure; (iii) financing of portfolio companies; (iv) floating rate borrowings of controlled portfolio companies; and (v) controlled portfolio company ownership.

General Partner or Limited Partner Clawbacks. As noted above, the SEC originally proposed to require current reporting for all private equity fund advisers within one business day of implementation of a general partner or limited partner clawback. The SEC instead adopted a new annual event reporting question in Section 4, which is only required for large private equity fund advisers. New Question 82 requires an adviser to indicate whether the reporting fund effectuated (i) any general partner clawback, or (ii) a limited partner clawback or clawbacks in excess of an aggregate amount equal to 10% of the fund's aggregate capital commitments. If so, the adviser is required to provide: (i) the effective date; (ii) whether it was a general partner or limited partner clawback; and (iii) the reason for the clawback.

A "general partner clawback" is defined to mean any obligation of the general partner, its related persons, or their respective owners or interest holders to restore or otherwise return performance-based compensation to the reporting fund pursuant to its governing documents. The required reporting for general partner clawbacks is triggered at the time the general partner becomes obligated to return to the fund performance-based compensation in excess of the amount it was ultimately entitled to receive under the fund's governing documents, regardless of when such compensation is actually returned.

A "limited partner clawback" is defined as any obligation of the fund's investors to return all or any portion of a distribution made by the reporting fund to satisfy a liability, obligation, or expense of the fund pursuant to the governing documents. Reporting is required with respect to limited partner clawbacks when the aggregate amount of such clawbacks over the course of the fund's life exceed 10% of the fund's aggregate capital commitments at such time. Once the threshold is met, advisers are required to file for each additional limited partner clawback, regardless of size (i.e., after meeting the threshold, the adviser would respond to this question in each subsequent annual filing if any limited partner clawback occurred during the preceding year). New Question 83 permits advisers to provide optional additional narrative information.

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Private Equity Fund Investment Strategies. New Question 66 was adopted as proposed and requires private equity fund advisers to select each reporting fund's investment strategy from a prescribed list. For funds that employ multiple strategies, the adviser must designate a good faith estimate of the percentage of deployed capital attributable to each strategy. Advisers may also select "other" and provide an explanation.

Fund-Level Borrowings. New Question 68 was adopted as proposed and requires advisers to report, with respect to any fund that engages in fund-level borrowing: (i) information regarding each borrowing or other cash financing available to the fund; (ii) the total dollar amount available; and (iii) the average amount borrowed over the reporting period. The Adopting Release notes that "other cash financing" is aimed at scenarios other than traditional borrowing where the fund has access to capital, including, for example, where the adviser agrees to provide cash to the fund.

Amendments to Existing Reporting Items. The SEC also adopted proposed amendments to the following existing reporting items.

Events of Default. Question 74 (redesignated as Question 77) is amended to require advisers to select from check boxes to identify the nature of a default event (i.e., payment default of the fund or a controlled portfolio company, or a default relating to failure to uphold terms of the applicable borrowing agreement).

Bridge Financing and Counterparties. Question 75 (redesignated as Question 78) is amended to require additional information about bridge financing providers and counterparties for controlled portfolio companies.

Geographic Information. Question 78 (redesignated as Question 67) is amended to require more specific geographic information on investments by private equity funds. Rather than reporting based on a prescribed list of regions and countries, advisers must list each country for which the fund's exposure is 10% or more of its net asset value, and provide the level of exposure as a percentage of net asset value.

Observations.

- As these questions are presented in Section 4 each year, we generally do not see a need for separate policies and procedures, although advisers may want to track any clawbacks to save time during a very busy April filing season.

- Unlike the quarterly reporting items, the compliance date for these reporting items will be one year from the publication in the federal register. Accordingly, most private equity fund advisers will not have to comply with these requirements until April 2025.

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