December 21, 2010

SEC Proposes New Rules to Implement Advisers Act Provisions of the Dodd-Frank Act — Implications for U.S. Advisers

On November 19, 2010, the U.S. Securities and Exchange Commission (the "SEC") proposed new rules and rule amendments[1] (the "Proposed Rules") under the Investment Advisers Act of 1940, as amended (the "Advisers Act") that are designed to give effect to the provision of Title IV of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") and, among other things:

- clarify the eligibility requirements for registration of investment advisers with the SEC and the transition process to state registration;
- address registration of investment advisers to hedge funds and other private funds with the SEC;
- amend Form ADV to, among other things, require disclosure of more information by investment advisers and the private funds they manage;
- implement the Dodd-Frank Act's mandate to require reporting by certain "exempt reporting advisers;"
- define "venture capital fund" for purposes of the exemption to SEC registration for investment advisers solely advising venture capital funds;
- provide clarity with respect to the exemptions to SEC registration for (i) investment advisers solely advising private funds and with aggregate regulatory assets under management ("AUM") of less than $150 million and (ii) "foreign private advisers;" and
- revise the SEC's recently promulgated "pay-to-play" rule.

Comments on the Proposed Rules are due by January 24, 2011.

Background

On July 21, 2010, President Obama signed into law the Dodd-Frank Act, which amends various provisions of the Advisers Act and requires or authorizes the SEC to adopt new rules and revise existing rules thereunder. Unless otherwise specifically provided for in the Dodd-

[1] See SEC Release No. IA-3110 entitled "Rules Implementing Amendments to the Investment Advisers Act of 1940" (November 19, 2010) at http://www.sec.gov/rules/proposed/2010/ia-3110.pdf (the "Implementing Release") and SEC Release No. IA-3111 entitled "Exemptions for Advisers to Venture Capital Funds, Private Fund Advisers With Less Than $150 Million in Assets Under Management, and Foreign Private Advisers" (November 19, 2010) at http://www.sec.gov/rules/proposed/2010/ia-3111.pdf (the "Exemptions Release").

Frank Act, the amendments made to the Advisers Act pursuant to Title IV of the Dodd-Frank Act become effective on July 21, 2011.

The amendments under the Dodd-Frank Act include the repeal of the "private adviser exemption" previously contained in Section 203(b)(3) of the Advisers Act, on which many investment advisers to hedge funds, private equity funds and venture capital funds had relied to remain exempt from SEC registration. As a result of the repeal, many investment advisers to "private funds"[2] will be required to register with the SEC and will be subject to SEC regulatory oversight, rules and examination. However, the Dodd-Frank Act also created, or directed the SEC to adopt, limited exemptions from registration for investment advisers to certain types of private funds. Certain categories of these investment advisers are, nevertheless, required to submit reports to the SEC. Further, in acknowledging the SEC's limited examination resources, the Dodd-Frank Act reallocated regulatory responsibility for smaller investment advisers to state securities authorities.

I. SEC-Registered Investment Advisers

A. Regulatory Assets Under Management Threshold

The Dodd-Frank Act amends Section 203A of the Advisers Act to effectively raise the AUM threshold for SEC registration to $100 million by creating a new category of investment advisers called "mid-sized adviser" which is defined as an investment adviser that (i) has AUM between $25 million and $100 million; (ii) is required to be registered[3] in the state where it maintains its principal office and place of business; and (iii) if so required to register, would be subject to examination[4] by such state. A mid-sized adviser generally may not register with the SEC,[5] unless such investment adviser would be required to register with 15 or more states or is an investment adviser to a registered investment company or a company which has elected to be a business development company pursuant to Section 54 of the Investment Company Act.[6]

Section 203A(a)(2) of the Advisers Act currently defines "assets under management" as the "securities portfolios with respect to which an investment adviser provides continuous and regular supervisory or management services." Current instructions to Form ADV provide

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2 A "private fund" is defined as any issuer that would be an investment company under Section 3 of the Investment Company Act of 1940, as amended (the "Investment Company Act"), but for the exception provided by either Section 3(c)(1) or Section 3(c)(7) thereunder.

3 For purposes of determining state registration status, the Implementing Release proposes to amend Form ADV, Part 1A to provide that "[i]f you are exempt from registration with that state or are excluded from the definition of investment adviser in that state, you must register with the SEC."

4 For purposes of determining state examination status, the SEC will contact each state securities commissioner (or official with similar authority) and request that each advise the SEC whether an investment adviser registered in the state would be subject to examination as an investment adviser by that state's securities commissioner (or agency or office with similar authority).

5 As a consequence, the SEC estimates that approximately 4,100 SEC-registered advisers will be required to withdraw their registrations and register with one or more state securities authorities.

6 The Implementing Release also proposes to amend Rule 203A-1 which currently provides most investment advisers with AUM between $25 million and $30 million an option to register either with the SEC or with the state(s). The Proposed Rule would eliminate this $5 million buffer in light of the new $100 million threshold, as well as certain other factors.

investment advisers with guidance in applying this provision, including a list of certain types of assets that investment advisers may (but are not required to) include. The SEC proposes revisions to Part 1A of Form ADV in order to implement a uniform method to calculate regulatory assets under management that would apply in determining whether an investment adviser is eligible to register with the SEC, as well as in determining similar calculations with respect to the exemptions for foreign private advisers and certain private fund advisers with less than $150 million in AUM. Specifically, the Implementing Release proposes requiring all investment advisers to include in their AUM securities portfolios for which they provide continuous and regular supervisory or management services, regardless of whether these assets are proprietary assets, assets managed without receiving compensation or assets of non-U.S. clients, all of which an investment adviser currently may exclude. In addition, an investment adviser may not subtract outstanding indebtedness and other accrued but unpaid liabilities, which remain in a client's account and are managed by the investment adviser. With respect to investment advisers to private funds, the SEC would require such an investment adviser to include in its AUM the fair value of any private fund over which it exercises continuous and regular supervisory or management services, regardless of the nature of the assets held by the fund, as well as the amount of any uncalled capital commitments made to the fund. If a private fund's governing documents provide for a specific process for calculating fair value (*e.g.*, the general partner has discretion over the determination of the fair value of the private fund's assets), then the adviser may rely on such process for calculating its AUM.

B. Additional Reporting Requirements for SEC-Registered Investment Advisers

Required Filing of Amendment to Form ADV. Proposed Rule 203A-5 would require every investment adviser registered with the SEC on July 21, 2011 to file an amendment to its Form ADV no later than August 20, 2011, 30 days after the effective date of Title IV of the Dodd-Frank Act, and to report the market value of its AUM determined within 30 days of the filing. This filing would be the first step by which an investment adviser no longer eligible for SEC registration would transition to state registration, requiring each investment adviser to determine whether it meets the revised eligibility criteria for SEC registration and providing the SEC and the state regulatory authorities with information necessary to identify those investment advisers required to transition to state registration.[7] An investment adviser no longer eligible for SEC registration would have to withdraw its SEC registration by filing Form ADV-W no later than October 19, 2011, 60 days after the required filing of an amendment to Form ADV. The SEC may cancel the registration of investment advisers that fail to file an amendment or withdraw their registrations in accordance with the Proposed Rules.

Changes to Form ADV Disclosures. The Implementing Release proposes to amend Form ADV to require, among other things, all registered investment advisers to provide more

[7] The Proposed Rules would amend Part 1A of Form ADV by requiring each investment adviser registered with the SEC (and each applicant for registration) to identify whether, under Section 203A, as amended, it is eligible to register with the SEC because it: (i) is a large investment adviser (having $100 million or more of AUM); (ii) is a mid-sized adviser that does not meet the criteria for state registration and examination; (iii) has its principal office and place of business in Wyoming (which does not regulate investment advisers) or outside the United States; (iv) meets the requirements for one or more of the exemptive rules under Section 203A; (v) is an investment adviser (or subadviser) to a registered investment company; (vi) is an investment adviser to a business development company and has at least $25 million of AUM; or (vii) has some other basis for registering with the SEC.

detailed information about: (i) their advisory business (including data about the types of clients they have, their employees and their advisory activities); (ii) their business practices that may present significant conflicts of interest (such as the use of affiliated brokers, soft dollar arrangements and compensation for client referrals); and (iii) their non-advisory activities and their financial industry affiliations.

To enhance its ability to oversee investment advisers to private funds, the SEC proposes requiring investment advisers to provide additional information on Form ADV about each private fund they manage. Specifically, the SEC proposes to amend Section 7B of Schedule D (which currently requires limited information about limited partnerships established by an investment adviser) to require investment advisers to private funds to provide expanded information about each private fund they advise, including:

- the name of the private fund;[8]
- the state or country where the private fund is organized;
- the name of the private fund's general partner, directors, trustees or persons occupying similar positions;
- the organization of the private fund, including whether it is a master or a feeder fund;
- the regulatory status of the private fund, including the exception from the Investment Company Act on which it relies;
- whether the fund relies on an exemption from registration of its securities under the Securities Act of 1933, as amended (the "Securities Act");
- whether the investment adviser is subject to a non-U.S. regulatory authority;
- whether the investment adviser is a subadviser to the private fund;
- the identity (by name and SEC file number) of any other investment advisers to the fund;
- the size of the private fund, including both its gross and net assets;
- the type of investment strategy employed by the investment adviser (to be selected from seven broad categories[9] which the applicable instruction would define);
- a breakdown of the assets and liabilities held by the private fund by class and categorization in the fair value hierarchy established under U.S. generally accepted accounting principles ("GAAP");[10]
- the number and the types of investors in the private fund;

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[8] The SEC proposes to add an instruction to this item to permit an investment adviser that seeks to preserve the anonymity of a private fund client by maintaining its identity in code in its records to identify the private fund in Schedule D using the same code.

[9] The categories include: (i) hedge fund; (ii) liquidity fund; (iii) private equity fund; (iv) real estate fund; (v) securitized asset fund; (vi) venture capital fund; and (vii) other private fund.

[10] The SEC notes that many private funds managed by investment advisers that would be reporting to the SEC prepare financial statements in accordance with GAAP. Others may use International Financial Reporting Standards requiring substantially similar information. Their adviser, therefore, should have access to this information from such financial statements.

- the minimum amounts required to be invested by fund investors;
- characteristics of the private fund that may present the investment adviser with conflicts of interest with fund investors of the sort that may implicate the investment adviser's fiduciary obligations to the private fund and, in some cases, create risks for the fund investors;
- whether clients of the investment adviser are solicited to invest in the private fund; and
- the percentage of the investment adviser's clients that have invested in the private fund.

This information is designed to provide the SEC with a comprehensive overview, or census, of private funds.

The Implementing Release would also amend Part B of this Section to require investment advisers to provide information regarding five categories of "gatekeepers" that perform critical roles for investment advisers and the private funds they manage, specifically, auditors, prime brokers, custodians, administrators and marketers. Such information includes: (i) the identity of each service provider; (ii) their location; (iii) whether they are related persons; (iv) specific information describing the services they provide; and (v) registration status (*e.g.*, for auditors, whether they are independent, registered with the Public Company Accounting Oversight Board and subject to its regular inspection, and whether audited statements are distributed to fund investors; for prime brokers, whether they are SEC-registered and whether they act as custodian for the private fund; for custodians, whether they are a related person of the investment adviser; for administrators, whether they prepare and send to investors account statements and what percentage of the private fund's assets are valued by the administrator or another person that is not a related person of the investment adviser; for marketers, whether they are related persons of the investment adviser, their SEC file number (if any), and the address of any website they use to market the private fund).

In addition, Item 7 currently requires each investment adviser to complete Section 7B of Schedule D for any "investment-related limited partnership" that the investment adviser or a related person advises. The SEC proposes to modify the scope of Item 7 by requiring completion of Section 7B for any "private fund" that the investment adviser advises. As a result, investment advisers must report all pooled investment vehicles regardless of whether they are organized as limited partnerships. In addition, investment advisers would no longer be required to report funds that are advised by affiliates, which in many cases would now be reported by an affiliate that is either registered under the Advisers Act or is now an exempt reporting adviser. To avoid multiple reporting for each private fund, the SEC is also proposing to permit a subadviser to exclude private funds for which an investment adviser is reporting on another Schedule D, and to permit an investment adviser sponsoring a master-feeder arrangement to submit a single Schedule D for the master fund and all of the feeder funds that would otherwise be submitting substantially identical data. Finally, the SEC proposes to permit an investment adviser with its principal office and place of business outside of the United States (a "non-U.S. adviser") to omit a Schedule D for a private fund that is not organized in the United States and that is not offered to, or owned by, a "United States

person."[11] This approach is designed to limit the reporting burden imposed on non-U.S. advisers with respect to funds in which U.S. investors have no direct interest.

In addition, the Implementing Release proposes to amend Form ADV to enable the SEC to identify those investment advisers that would be subject to Section 956 of the Dodd-Frank Act which requires the SEC, jointly with certain other federal regulators, to adopt rules or guidelines addressing certain excessive incentive-based compensation arrangements, including those of investment advisers with $1 billion or more in assets. The proposal would require an investment adviser to indicate in Part IA of Form ADV whether or not the investment adviser had $1 billion or more in assets as of the last day of the investment adviser's most recent fiscal year. For these purposes, the amount of assets would be the investment adviser's total assets (*e.g.*, the total assets of the advisory firm rather than the total regulatory assets under management) determined in the same manner as the amount of "total assets" is determined on the investment adviser's balance sheet for its most recent fiscal year end.

Books and Records Requirements for Newly Registered Investment Advisers. The SEC proposes to amend Rule 204-2, the "books and records" rule, to update the rule's grandfathering provision for investment advisers that are currently exempt from registration under the "private adviser exemption," but will be required to register when the Dodd-Frank Act's elimination of this exemption becomes effective on July 21, 2011. At that time, these investment advisers would become subject to the recordkeeping requirements of the Advisers Act, including the requirement to keep certain records relating to performance. Under the proposed amendments to Rule 204-2, an investment adviser that was, prior to July 21, 2011, exempt from registration pursuant to the "private adviser exemption" (and did not actually register with the SEC) would not be required to maintain or preserve books and records that would otherwise be required to be maintained or preserved under the Rule to the extent those books and records pertain to the performance or rate of return of such private fund or other account advised by such investment adviser for any period ended prior to July 21, 2011; however, to the extent that the investment adviser preserved these performance-related records without being required to do so by current Rule 204-2, the proposed grandfathering provision would require it to continue to preserve them.

II. Exempt Reporting Advisers

As noted above, the Dodd-Frank Act created new exemptions from registration for certain types of investment advisers; however, these exemptions are not mandatory. Thus, an investment adviser that qualifies for any of the exemptions could choose to register (or remain registered) with the SEC, subject to the other provisions of Section 203A of the Advisers Act. The Exemptions Release provides that subadvisers may rely on each of the new exemptions, provided that any such subadviser satisfies all of the terms and conditions of the applicable Proposed Rule(s).

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[11] A "United States person" is generally defined by incorporating the definition of a "U.S. person" contained in Regulation S (Rules 901 through 905 of the Securities Act). Regulation S looks generally to the residence of an individual to determine whether the individual is a United States person. Regulation S generally treats legal partnerships and corporations as United States persons if they are organized or incorporated in the United States, and trusts by reference to the residence of the trustee. It treats discretionary accounts generally as United States persons if the fiduciary is a resident of the United States.

A. Venture Capital Exemption

The Dodd-Frank Act amended the Advisers Act to exempt investment advisers that solely advise venture capital funds from registration, and directed the SEC to define the term "venture capital fund." An investment adviser would be eligible to rely on the venture capital exemption only if it solely advises venture capital funds that meet all of the elements of the proposed definition or if it were grandfathered.

Proposed Rule 203(l)-1 would define a "venture capital fund" as a "private fund"[12] that: (i) represents to investors and potential investors that it is a venture capital fund; (ii) owns solely (x) equity securities[13] issued by one or more "qualifying portfolio companies," and at least 80% of the equity securities of each qualifying portfolio company owned by the fund was acquired directly from the qualifying portfolio company; and (y) cash and cash equivalents and U.S. Treasuries with a remaining maturity of 60 days or less; (iii) directly, or through its investment advisers, offers or provides significant managerial assistance to, or controls,[14] the qualifying portfolio company; (iv) does not borrow, issue debt obligations, provide guarantees or otherwise incur leverage, in excess of 15% of the private fund's aggregate capital contributions and uncalled committed capital, and any such borrowing, indebtedness, guarantee or leverage is for a non-renewable term of no longer than 120 calendar days; (v) does not offer its investors redemption or other similar liquidity rights except in extraordinary circumstances; and (vi) is not registered under the Investment Company Act and has not elected to be treated as a business development company.

A "qualifying portfolio company" would be defined generally as any company that: (i) at the time of fund investment, is not publicly traded (nor could it control, be controlled by, or be under common control with, a publicly traded company);[15] (ii) does not incur leverage in connection with the investment by the private fund; (iii) uses the capital provided by the fund for operating or business expansion purposes rather than to buy out other investors; and (iv) is not itself a private fund or other pooled investment vehicle (*i.e.*, it is an operating company).

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12 See *supra* note 2.

13 The Exemptions Releases proposes to use the definition of equity security contained in Section 3(a)(11) of the Securities Exchange Act of 1934, as amended, and Rule 3a11-1 thereunder. Section 3(a)(11) defines an equity security as "any stock or similar security; or any security future on any such security; or any security convertible, with or without consideration, into such a security, or carrying any warrant or right to subscribe to or purchase such a security; or any such warrant or right; or any other security which the Commission shall deem to be of similar nature and consider necessary or appropriate, by such rules and regulations as it may prescribe in the public interest or for the protection of investors, to treat as an equity security." Rule 3a11-1 defines an equity security to include "any stock or similar security, certificate of interest or participation in any profit sharing agreement, preorganization certificate or subscription, transferable share, voting trust certificate or certificate of deposit for an equity security, limited partnership interest, interest in a joint venture, or certificate of interest in a business trust; any security future on any such security; or any security convertible, with or without consideration into such a security, or carrying any warrant or right to subscribe to or purchase such a security; or any such warrant or right; or any put, call, straddle, or other option or privilege of buying such a security from or selling such a security to another without being bound to do so."

14 The Exemptions Release does not define "control" for this purpose.

15 However, a venture capital fund could continue to hold securities of a portfolio company that subsequently becomes public.

Under a "grandfathering provision," the Exemptions Release proposes that an investment adviser may treat any existing private fund as a venture capital fund for purposes of Section 203(l) of the Advisers Act if the fund meets the following elements of the grandfathering provision: (i) represented to investors and potential investors at the time the fund offered its securities that it is a venture capital fund; (ii) has sold securities to one or more investors prior to December 31, 2010; and (iii) does not sell any securities to, including accepting any additional capital commitments from, any person after July 21, 2011. In providing the grandfathering provision, the SEC acknowledges that requiring existing venture capital funds to modify their investment conditions or characteristics, liquidate portfolio company holdings or alter the rights of investors in the funds in order to satisfy the proposed definition of a venture capital fund would likely be impossible in many cases and yield unintended consequences for the funds and their investors. The Exemptions Release clarifies that a fund that "represents" itself to investors as a venture capital fund is typically one that discloses it pursues a venture capital investing strategy and identifies itself as such; thus, the SEC does not expect funds identifying themselves as a "private equity" or "hedge" fund would be able to rely on this exemption.

B. Private Fund Adviser Exemption

The Dodd-Frank Act amends Section 203(m) of the Advisers Act by directing the SEC to exempt from registration any investment adviser that solely advises private funds and that has aggregate AUM in the United States of less than $150 million (the "private fund adviser exemption"). The Exemptions Release proposes Rule 203(m)-1 which limits an investment adviser with its principal office and place of business[16] in the United States (a "U.S. adviser") relying on the exemption to solely advising "qualifying private funds."[17] If such an investment adviser acquires a different type of client, the investment adviser would no longer be able to rely on the private fund adviser exemption. All of the qualifying private fund assets of a U.S. adviser would be deemed to be "assets under management in the United States," although day-to-day management of certain assets may also take place at another location. Proposed Rule 203(m)-1 would require investment advisers to calculate AUM by reference to Item 5F of Form ADV (pursuant to the newly proposed calculation method described above), which is intended to provide a uniform method of calculating assets under management for regulatory purposes under the Advisers Act. For purposes of this calculation, qualifying private fund assets are calculated as the fair value of such assets as of the end of each calendar quarter.

For a discussion of applicability of the private fund adviser exemption to a non-U.S. adviser, see the Paul, Weiss Client Memorandum entitled, "*SEC Proposes New Rules to Implement Advisers Act Provisions of the Dodd-Frank Act — Implications for Non-U.S. Advisers*."

Proposed Rule 203(m)-1 also includes a provision giving an investment adviser one calendar quarter (three months) to register with the SEC after becoming ineligible to rely on the private

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[16] "Principal office and place of business" of an investment adviser means the executive office of the investment adviser from which the officers, partners or managers of the investment adviser direct, control and coordinate the activities of the investment adviser.

[17] A "qualifying private fund" is defined as any "private fund" (see *supra* note 2) that is not registered under Section 8 of the Investment Company Act and has not elected to be treated as a business development company.

fund adviser exemption due to an increase in the value of its qualifying private fund AUM. This three month period is intended to enable the investment adviser to take steps to register and otherwise come into compliance with the requirements of the Advisers Act applicable to registered investment advisers, including the adoption and implementation of compliance policies and procedures.

C. Reporting Requirements for Exempt Reporting Advisers

Congress gave the SEC broad authority to require investment advisers solely advising venture capital funds and investment advisers solely advising private funds and having aggregate AUM in the United States of less than $150 million (such investment advisers, "exempt reporting advisers") to file reports "as the Commission determines necessary or appropriate in the public interest or for the protection of investors."

Under the Implementing Release, exempt reporting advisers would be required to file, and periodically update, Form ADV (renamed as the "Uniform Application for Investment Adviser Registration and Reporting Form By Exempt Reporting Advisers") on the SEC's investment adviser electronic filing system (the Investment Adviser Registration Depository), and these reports would be publicly available on the SEC's website. However, rather than completing all of the items on Part 1A of Form ADV, exempt reporting advisers would fill out a limited subset of items,[18] including:

- basic identification details about an exempt reporting adviser such as name, address, contact information, form of organization, the identity of its owners and affiliates and the exemption(s) that it is relying on to report, rather than register, with the SEC (Items 1 (Identifying Information), 2C (SEC Reporting by Exempt Reporting Advisers), 3 (Form of Organization) and 10 (Control Persons) and corresponding sections of Schedules A, B and C);
- details about the private funds the investment adviser manages and about other business activities that the investment adviser and its affiliates are engaged in that present conflicts of interest that may suggest significant risk to clients (Items 6 (Other Business Activities) and 7 (Financial Industry Affiliations and Private Fund Reporting) and corresponding sections of Schedule D); and
- the disciplinary history of the investment adviser and its employees that may reflect on their integrity (Item 11 (Disclosure Information)).

Because exempt reporting advisers manage private funds, the SEC proposes to require them to complete the expanded information required by Item 7B and Section 7B of Schedule D for each private fund they advise, as discussed above.

An exempt reporting adviser would be required to file its initial report with the SEC on Form ADV no later than August 20, 2011, 30 days after the effective date of Title IV of the Dodd-Frank Act. Proposed amendments to Rule 204-1 would require an exempt reporting adviser

[18] Exempt reporting advisers would not be required to complete the remaining items of Part IA or prepare a client brochure on Form ADV Part 2. In addition, although exempt reporting advisers would be instructed to provide answers only to those items noted above, the SEC is not proposing to change the content of the items required for exempt reporting advisers.

to amend its Form ADV: (i) at least annually, within 90 days of the end of the investment adviser's fiscal year; and (ii) promptly, if the information in Items 1 (Identification Information), 3 (Form of Organization), or 11 (Disciplinary Information) becomes inaccurate in any way, and to update Item 10 (Control Persons) if it becomes materially inaccurate.

D. SEC Examination and Oversight

Importantly, the Implementing Release takes the position[19] that exempt reporting advisers are entirely subject to Section 204 of the Advisers Act, the result of which is that such investment advisers will be subject to examination by the SEC, as well as subject to the other reporting and recordkeeping[20] provisions of the Advisers Act. In her prepared statement during the SEC's Open Meeting on November 19th, Commissioner Kathleen Casey indicated that there was ambiguity in the statutory language of the Dodd-Frank Act as to whether this was the proper reading of Congress's intention. Commissioner Casey stated, "I believe a better reading is that Congress sought to exempt these advisers from the registration framework, but then provided the Commission with the limited authority to require reporting and recordkeeping, as we determined was necessary and appropriate. . . . I believe that with this release we have eroded the significance of being exempted from registration so far as to make it a distinction without a difference. This seems a rather odd result given Congress's apparent interest in exempting these advisers from the regulatory burdens associated with registration under the Advisers Act." Commissioner Casey was the only Commissioner who voted against proposing the Implementing Release.

III. Foreign Private Adviser Exemption

The Dodd-Frank Act amends Section 203(b)(3) of the Advisers Act to provide for an exemption from registration for "foreign private advisers" defined as any investment adviser that: (i) has no place of business in the United States; (ii) has, in total, fewer than 15 clients in the United States and investors in the United States in private funds advised by the investment adviser; (iii) has aggregate assets under management attributable to clients in the United States and investors in the United States in private funds advised by the investment adviser of less than $25 million; and (iv) does not hold itself out generally to the public in the United States as an investment adviser. For a discussion of Proposed Rule 202(a)(30)-1, which seeks to define certain terms included in the statutory definition of "foreign private adviser" in order to clarify application of the exemption, see the Paul, Weiss Client Memorandum entitled, "*SEC Proposes New Rules to Implement Advisers Act Provisions of the Dodd-Frank Act — Implications for Non-U.S. Advisers*."

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[19] The Exemptions Release states in footnote 30, "Under section 204(a) of the Advisers Act, the Commission has the authority to require an investment adviser to maintain records and provide reports, as well as the authority to examine such adviser's records, unless the adviser is 'specifically exempted' from the requirement to register pursuant to section 203(b) of the Advisers Act. Investment advisers that are exempt from registration in reliance on section 203(l) or 203(m) of the Advisers Act are not 'specifically exempted' from the requirement to register pursuant to section 203(b), and thus the Commission has authority under section 204(a) of the Advisers Act to require those advisers to maintain records and provide reports and has authority to examine such advisers' records."

[20] The Implementing Release indicates that recordkeeping requirements for exempt reporting advisers will be addressed in a future SEC release.

IV. Amendments to the SEC Pay-to-Play Rule

The SEC is also proposing to amend Rule 206(4)-5 of the Advisers Act, the investment adviser "pay-to-play" rule, in response to changes made by the Dodd-Frank Act. The pay-to-play rule generally prohibits registered and certain unregistered investment advisers from engaging directly or indirectly in pay-to-play practices identified in the rule.

The Proposed Rules would amend the scope of the pay-to-play rule to make it applicable to exempt reporting advisers and foreign private advisers.

Also, under the proposed amendments to Rule 206(4)-5, an investment adviser would be permitted to pay a "regulated municipal advisor," instead of a "regulated person," to solicit government entities on its behalf if the municipal advisor is subject to a pay-to-play rule adopted by the Municipal Securities Rulemaking Board ("MSRB") that is at least as stringent as the Advisers Act pay-to-play rule. The Dodd-Frank Act created a new category of person known as a "municipal advisor," which it defines to include persons that undertake "a solicitation of a municipal entity." These persons include, among others, any third-party solicitor, including registered investment advisers and broker-dealers, seeking business on behalf of an investment adviser from a municipal entity, including a pension fund. These municipal advisors are subject to MSRB rules, and the SEC indicated that it understands that the MSRB intends to consider subjecting municipal advisors to pay-to-play rules similar to its rules governing municipal securities dealers. Broker-dealers acting as placement agents or solicitors and investment advisers acting as solicitors of municipal entities and obligated persons generally meet the statutory definition of a municipal advisor and thus would be subject to MSRB rules. The proposed amendment would, like the current rule, permit investment advisers to pay persons to solicit government entities on their behalf only if such third parties are registered with the SEC and subject to pay-to-play rules. Given the new regulatory regime applicable to municipal advisors, including solicitors of government entities that meet the definition of "regulated person" under rule 206(4)-5, broker-dealer solicitors are expected to be subject to MSRB's pay-to-play rules, rendering it unnecessary at this time for the Financial Industry Regulatory Authority ("FINRA") to adopt a pay-to-play rule that would satisfy rule 206(4)-5(f)(9)(ii). The SEC proposes, therefore, to replace references in rule 206(4)-5 to FINRA's pay-to-play rules with references to MSRB rules that the SEC finds are consistent with the objectives of Rule 206(4)-5 and impose substantially equivalent or more stringent pay-to-play restrictions.

Finally, the SEC proposes an amendment to Rule 206(4)-5's definition of a "covered associate" to clarify that a legal entity, in addition to a natural person, that acts as the general partner or managing member of an investment adviser would fall within such definition. This proposed amendment is not related to the Dodd-Frank Act, but is instead meant to clarify the rule and the SEC's original intent in adopting Rule 206(4)-5 that "covered associate" include legal entities, as well as natural persons, and to respond to questions received by the SEC staff with respect to the interpretation of that definition.

V. Important Filing Deadlines

August 20, 2011 – Every investment adviser registered with the SEC on July 21, 2011 must file an amendment to its Form ADV containing information necessary to identify whether the investment adviser must transition to state registration or continue with SEC registration.

August 20, 2011 – Each "exempt reporting adviser" must file its initial report with the SEC on Form ADV.

October 19, 2011 – Any investment adviser no longer eligible for SEC registration must withdraw its SEC registration by filing Form ADV-W with the SEC.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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Appendix I

Newly Proposed Rules Implementing Advisers Act Provisions of the Dodd-Frank Act		
Type of Investment Adviser	**Description**	**Reporting Requirements and Filing Deadlines**
SEC-Registered (or required to be registered) IAs	an IA that • is a large IA (having $100 million or more of AUM); • is a mid-sized IA that does not meet the criteria for state registration and examination; • has its principal office and place of business in Wyoming (which does not regulate IAs) or outside the United States; • meets the requirements under one or more of the exemptions from prohibition on SEC registration under Rule 203A (*e.g.*, pension consultants); • is an IA (or subadviser) to a registered investment company; • is an IA to a business development company and has at least $25 million of AUM; or • has some other basis for registering with the SEC	**August 20, 2011** –Amendment to Form ADV due with respect to every IA registered with the SEC on July 21, 2011, including new calculation of regulatory AUM and more detailed information about advisory business, conflicts of interest, non-advisory activities, financial industry affiliations, private funds advised and service providers to such private funds If IA was, prior to July 21, 2011, exempt from registration pursuant to the "private adviser exemption" (and did not actually register with the SEC), IA not required to maintain or preserve books and records pertaining to the performance or rate of return of such private fund or other account advised by such investment adviser for any period ended prior to July 21, 2011; however, to the extent that the IA preserved these performance-related records without being required to do so by current Rule 204-2, such an IA required to continue to preserve them Amendments to Form ADV required: • at least annually, within 90 days of the end of the IA's fiscal year; or • more frequently if specifically required by the instructions to Form ADV
Mid-Sized IAs	an IA that • has AUM between $25 million and $100 million; • is required to be registered in the state where it maintains its principal office and place of business; and • if so required to register, would be subject to examination by such state	**August 20, 2011** –Amendment to Form ADV due with respect to every IA registered with the SEC on July 21, 2011, including new calculation of regulatory AUM and more detailed information about advisory business, conflicts of interest, non-advisory activities, financial industry affiliations, private funds advised and service providers to such private funds **October 19, 2011** – Form ADV-W due withdrawing such an IA's SEC registration; prior to such date, applicable state registration(s) must be completed, including acquiring any relevant licenses and taking any relevant examinations
Venture Capital IAs	an IA that solely advises venture capital funds, defined as a private fund that: • represents to investors and potential investors that it is a venture capital fund; • owns solely (x) equity securities issued by one or more "qualifying portfolio companies," and at least 80% of the equity securities of each qualifying portfolio company owned by the fund was acquired directly from the qualifying portfolio company; and (y) cash and cash equivalents and U.S. Treasuries with a remaining maturity of	**August 20, 2011** – subset of Part 1A of Form ADV due (specifically, Items 1, 2C, 3, 6, 7, 10 and 11 and Schedules A, B, C and D) Amendments to Form ADV required: • at least annually, within 90 days of the end of the IA's fiscal year; or • more frequently if specifically required by the instructions to Form ADV

Appendix I

Newly Proposed Rules Implementing Advisers Act Provisions of the Dodd-Frank Act		
Type of Investment Adviser	**Description**	**Reporting Requirements and Filing Deadlines**
	Treasuries with a remaining maturity of 60 days or less; • directly, or through its investment advisers, offers or provides significant managerial assistance to, or controls, the qualifying portfolio company; • does not borrow, issue debt obligations, provide guarantees or otherwise incur leverage, in excess of 15% of the private fund's aggregate capital contributions and uncalled committed capital, and any such borrowing, indebtedness, guarantee or leverage is for a non-renewable term of no longer than 120 calendar days; • does not offer its investors redemption or other similar liquidity rights except in extraordinary circumstances; and • is not registered under the ICA and has not elected to be treated as a business development company; or • pursuant to a grandfathering provision, a private fund that: (i) represented to investors and potential investors at the time the fund offered its securities that it is a venture capital fund; (ii) has sold securities to one or more investors prior to December 31, 2010; and (iii) does not sell any securities to, including accepting any additional capital commitments from, any person after July 21, 2011	
Private Fund IAs	an IA that: • solely advises private funds; and • has aggregate AUM in the United States of less than $150 million	**August 20, 2011** – subset of Part 1A of Form ADV due (specifically, Items 1, 2C, 3, 6, 7, 10 and 11 and Schedules A, B, C and D) Amendments to Form ADV required: • at least annually, within 90 days of the end of the IA's fiscal year; or • more frequently if specifically required by the instructions to Form ADV
Foreign Private IAs	an IA that: • has no place of business in the United States; • has a total of fewer than 15 clients in the United States and investors in the United States in private funds advised by the adviser; • has aggregate AUM attributable to clients and investors in the United States in private funds advised by such adviser of less than $25 million; and does not hold itself out generally to the U.S. public	None