



NEW HEDGE FUND LEGISLATION INTRODUCED IN U.S. SENATE

Senator Reed proposes Private Fund Transparency Act

Concurrently with the release of President Obama's financial regulatory reform plan, Senator Jack Reed (D-RI), introduced a bill (S. 1276) aimed at regulating the hedge fund industry. The bill, entitled The Private Fund Transparency Act of 2009, would amend the Investment Advisers Act of 1940, as amended (the "Advisers Act") to require advisers (other than foreign private advisers) to hedge funds, private equity funds, venture capital funds, and other private investment pools to register with the Securities and Exchange Commission ("SEC").

Further details on the bill are provided below.

Private Fund Transparency Act of 2009

The Private Fund Transparency Act of 2009¹ would amend Section 203(b)(3) of the Advisers Act. Section 203(b)(3), which is more commonly known as the "private adviser exemption," is the exemption upon which most (if not all) unregistered hedge funds managers currently rely to avoid registration with the SEC.² Under (current) Section 203(b)(3), an investment adviser is not required to register with the SEC if it:

- has had fewer than 15 clients during the preceding 12 months;
- does not hold itself out to the public as an investment adviser; and
- does not advise any registered investment companies, such as mutual funds, or companies electing to be regulated as business development companies.

If passed, Senator Reed's bill would delete Section 203(b)(3) in its entirety and replace it with the phrase "any adviser that is a foreign private adviser", thus rendering the private adviser exemption unavailable for all private fund advisers unless they fit within the narrow definition of "foreign private adviser". Under Senator Reed's bill, a "foreign private adviser" is defined as an adviser that does not have a place of business in the United States, has had fewer than fifteen clients who are U.S. persons within the past twelve months, and have less than \$25 million of assets under management attributable to client in the United States. The bill does not contain any specific guidance on what would constitute a "client" under the definition of foreign private adviser, i.e., the fund itself or the fund's underlying investors, or whether a U.S.-domiciled private investment

¹ See <http://thomas.loc.gov/cgi-bin/query/z?c111:s1276>: for a copy of the full text of the Private Fund Transparency Act of 2009.

² We note that hedge fund managers currently exempt from registration under Section 203(b)(3) of the Advisers Act are nonetheless subject to a number of the Advisers Act provisions, including the antifraud provisions. However, registered investment advisers become subject to all provisions of the Advisers Act, including requirements regarding annual disclosure, compliance policies and procedures, code of ethics, proxy voting rules and recordkeeping.

fund with a majority of non-U.S. investors could be subject to a look-through for purposes of determining the number of clients.

The bill retains the current of \$30 million minimum assets under management threshold for requiring private fund advisers to register with the SEC. Thus if passed, the Private Fund Transparency Act of 2009 would require all advisers to private funds (other than foreign private advisers) that manage more than \$30 million in assets to register as investment advisers with the SEC unless they can rely on another exemption (which is unlikely). In addition, the Private Fund Transparency Act of 2009 (if passed) would:

- provide the SEC with the authority to collect information from the hedge fund industry and other investment pools, including the risks they may pose to the financial system;
- authorize the SEC to require hedge funds and other investment pools to maintain and share with other federal agencies any information necessary for the calculation of systemic risk; and
- clarify the SEC's regulatory authority with respect to recordkeeping and confidential reporting by private funds and their advisers in order to strengthen its ability to oversee registered investment advisers.

Specifically, the bill clarifies that for purposes of the Advisers Act recordkeeping requirement, the records of an investment company advised by an investment adviser are deemed to be the records of the investment adviser with respect to any investment company relying on Section 3(c)(1) or Section 3(c)(7) to avoid registration under the Investment Company of 1940, as amended. The bill also removes certain restrictions under the Advisers Act on the SEC's ability to collect information from private fund advisers.

We note that as described in previous HedgeOp Client Alerts, other proposed hedge fund bills are currently pending in both the U.S. Senate and the U.S. House of Representatives. We will continue to monitor closely the proposed federal legislation and we will keep you apprised of any further developments.

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