

**> Guide To SEC Investment Adviser
Registration For Hedge Fund And
Private Equity Fund Managers**

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Introduction

“It was the best of times, it was the worst of times”. While a cliché, we think that this is a fairly accurate description of the current hedge fund and private equity fund industries. As the managers of these types of funds, you are expected to maintain returns and be nimble in the face of changing markets, while complying with looming new regulatory burdens. While we cannot help with returns, we can help make the regulatory process easier to navigate and understand.

Many of you will be required to register with the SEC as investment advisers. We have prepared this guide to assist you in registering. We have broken down our discussion into three main sections. The first section is a summary in question and answer format of the key points that you should think about when you are registering. The second section provides more detail on the registration process and includes various requirements applicable to SEC-registered advisers, as well as certain general state requirements. The third section provides a timeline to assist you in registering.

And unlike Dickens, we have tried to be as brief as possible.

Please note that this guide is intended as a general summary of certain SEC investment adviser registration considerations for hedge fund and private equity fund managers only and is not intended as legal advice on any particular set of circumstances. This guide does not discuss registration as an investment adviser with any state securities regulator or regulatory authority other than the SEC. You should consult with counsel as to all registration-related and other legal and compliance matters.

Summary FAQs

Q: When am I required to register with the SEC as an investment adviser?

You are required to register with the SEC under the Investment Advisers Act (the “Advisers Act”) if:

- you have regulatory assets under management of \$150 million or more;
- some of your clients are not hedge funds or private equity funds, and you have regulatory assets under management of \$100 million or more;
- some of your clients are not hedge funds or private equity funds, you have regulatory assets under management of \$25 million or more and your principal office and place of business is in a state where either: (i) you are not required to register with the state securities regulator as an investment adviser; or (ii) you are required to register with, but you are not subject to examination as an investment adviser by, the state securities regulator (currently, the only states where you are not subject to examination are New York and Wyoming); or

- you act as an adviser to a registered investment company or a business development company, or you hold yourself out to the public in the United States as an investment adviser.

You are not required to register if:

- you have regulatory assets under management of less than \$25 million, subject to certain exceptions (note that you may still be required to register in the states in which you do business);
- you advise only venture capital funds ¹;
- you are a “foreign private adviser” (which is discussed below); or
- you are registered with the CFTC as a commodity trading advisor and your business is not predominantly the provision of securities-related advice.

Note that there are a variety of other exemptions and exclusions that are not generally available for hedge fund or private equity fund managers, such as an exclusion for family offices.

For purposes of assessing whether you are eligible to register (or qualify for an exemption, or are prohibited, from registration), the SEC requires that you determine your “regulatory assets under management” by calculating the value of the securities portfolios with respect to which you provide continuous and regular supervisory or management services. Your regulatory assets under management include: (i) proprietary assets; (ii) assets managed without receiving compensation; (iii) assets of foreign clients; and (iv) uncalled capital commitments. In addition, you are not permitted to subtract outstanding indebtedness (including leverage) and other accrued but unpaid liabilities, and must value assets at their market value, or fair value where market value is unavailable. You are required to calculate the amount of your regulatory assets under management annually to confirm whether you exceed a threshold for registration. After reaching the threshold, you will then generally have up to 90 days to register with the SEC (unless you are otherwise exempt from registration).

¹ Rule 203(l)-1 defines a “venture capital fund” generally as any private fund that: (1) represents to investors that it pursues a venture capital strategy; (2) immediately after the acquisition of any asset, other than qualifying investments or short-term holdings (as defined in the rule), holds no more than 20% of the amount of the fund’s aggregate capital contributions and uncalled committed capital in assets (other than short-term holdings) that are not qualifying investments, valued at cost or fair value, consistently applied by the fund; (3) 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, except that any guarantee by the private fund of a qualifying portfolio company’s obligations up to the amount of the value of the private fund’s investment in the qualifying portfolio company is not subject to the 120 calendar day limit; (4) only issues securities the terms of which do not provide a holder with any right, except in extraordinary circumstances, to withdraw; and (5) is not registered under section 8 of the Investment Company Act and has not elected to be treated as a business development company pursuant to section 54 of the Investment Company Act.

Certain advisers that are not required to register are still subject to certain recordkeeping and reporting obligations.

Q: My principal office and place of business is outside the U.S. When am I required to register as an investment adviser?

The Dodd-Frank Act added a new exemption from SEC registration for a “foreign private adviser”, which is an investment adviser that: (i) has no place of business in the U.S.; (ii) has fewer than 15 clients and fund investors in the U.S.; (iii) has less than \$25 million in regulatory assets under management from clients and fund investors in the U.S.; (iv) does not hold itself out to the public in the U.S. as an investment adviser; and (v) does not act as an investment adviser to a registered investment company or a business development company. You must register with the SEC if you do not meet all of these requirements, unless there is another exemption available.

Even if you do not qualify as a foreign private adviser, you may rely on the exemption for advisers solely advising hedge funds and private equity funds if: (i) all of your U.S. person clients are hedge funds and private equity funds, without regard to the type of non-U.S. clients, and (ii) the value of all assets that you manage from a place of business in the United States are solely attributable to hedge funds and private equity funds, and their aggregate fair value is less than \$150 million.

Please note that, if you are registered with the SEC, you are not required to comply with many of the substantive requirements of the Advisers Act with respect to your non-U.S. clients (including non-U.S. funds in which U.S. persons invest). Under this “regulation lite” regime, you are generally required to maintain certain books and records and make yourself or your records available to examination by SEC staff. While the Dodd-Frank Act and SEC rules do not specifically address “regulation lite”, the SEC has indicated that it is not withdrawing any existing guidance, and, therefore, it is reasonable to expect that the “regulation lite” regime will continue.

Q: I am not required to register with the SEC. May I register anyway?

Generally speaking, investment advisers must register with the SEC or one or more states and may not choose with whom they can register, subject to certain exceptions.

If you are exempt from SEC registration because: (i) you advise solely hedge funds and/or private equity funds and have regulatory assets under management of less than \$150 million; (ii) you advise solely venture capital funds; or (iii) are a “foreign private adviser”, you may elect to register with the SEC, unless you are prohibited from registering.

If you have between \$25 million and \$100 million of regulatory assets under management and: (i) you are required to be registered as an investment adviser in the state in which you maintain your principal office and place of business; and (ii) if registered, you would be subject to examination as an investment adviser by the applicable state securities commissioner, you will not be permitted to register with the SEC, unless you are required to register with 15 or more states. Currently, the only

states that do not meet these requirements are New York and Wyoming. Accordingly, if you have between \$25 million and \$100 million of regulatory assets under management and maintain your principal office and place of business in New York or Wyoming, you must register with the SEC (unless another exemption is available). If you have less than \$25 million in regulatory assets under management, you are also prohibited from registering with the SEC, subject to certain exceptions. State rules vary considerably, and you should consult with counsel as to your particular circumstances.

Q: What do I need to do before I register?

At the time your registration becomes effective (note that you will have no control over when this happens once you file your Form ADV), your business and operations must be fully compliant with the Advisers Act. **There is no grace period after the date you are registered.** Accordingly, before you file your application to register on Form ADV, you should make sure that your business and operations comply with the Advisers Act (this may include enhancing your operations by, among other things, purchasing and installing new software to capture all of your records and emails).

In our experience, the compliance item that requires the most lead time is building out your compliance manual and infrastructure. You will need to adopt and implement policies and procedures reasonably designed to prevent violations of the Advisers Act, and designate a Chief Compliance Officer to be responsible for developing and enforcing these policies and procedures. Policies and procedures must be tailored to your specific structure, investment strategy and operations, and need to reflect your actual practices. **You should not adopt an off-the-rack compliance manual.** Adopting an off-the-rack compliance manual may impose on your business unnecessary or inappropriate compliance burdens. Your compliance procedures should be reviewed internally and tested prior to being implemented to make sure they are effective.

You should prepare Part 1 and Part 2 of Form ADV. Part 1 requires general information about your business, details about the persons that own or control your business and biographical information about you and your key investment professionals, and Part 2 requires more detailed information about your operations and advisory personnel. You will likely need to gather information from your employees to complete the form. Once the form has been completed, we recommend that it be reviewed by your legal counsel. Note that Part 1 of Form ADV requires disclosure of information relating to each hedge fund and private equity fund you advise, including information on service providers.

Before you register, you will likely need to make other changes to your business and operations to make sure that they comply with the Advisers Act. For example, once you are registered, you are only allowed to charge a performance fee to clients (including investors in 3(c)(1) funds) that are “qualified clients”² (note, however, that existing

² Generally, a qualified client is a natural person or company that: (i) immediately after entering into an advisory contract with the adviser, has at least \$1 million under management with the adviser; (ii) the adviser reasonably believes has a net worth of \$2 million (together, in the case of a natural person, with

arrangements with clients and investors as of the date you register are grandfathered for purposes of this rule). In addition, your pitchbooks and other marketing materials must comply with the SEC's rules regarding advertisements. We have included a general summary of the Advisers Act and its rules in the "Guide to Registration" section below.

Finally, you should review your offering documents, fund subscription agreements, advisory agreements, counterparty agreements (including ISDAs) and other legal documents. You should determine whether you will need to notify any person or firm that you are registering. You also may need to update these documents to make them compliant with the Advisers Act, and you should determine whether your registration triggers any other provisions of these documents. You should also plan on updating these documents to reflect your registration.

Q: How do I register?

To register, you must electronically file Form ADV with the SEC through the Investment Adviser Registration Depository ("IARD"), the registration system managed by the Financial Industry Regulatory Authority ("FINRA").

To open an IARD user account, you will need to complete an IARD Entitlement Packet (available at <http://www.iard.com/pdf/secEntitlementPacket.pdf>) and mail it to FINRA. This process can take up to 2 weeks, though it normally takes just a few days. Prior to registration, you will need to pre-fund your IARD account to pay for your initial set-up fee. The initial set-up fee will be based on your assets under management. If you are required to make notice filings with certain states (which is typically based on whether or not you have an office in that state or the number of clients you have in that state), you will also be required to fund your account with the amount of the state filing fees.

The next step is to complete and file Form ADV through the IARD system. Part 1 of Form ADV is completed electronically on the IARD system and Part 2A of Form ADV must be attached as a PDF exhibit to Part 1. Part 1 and Part 2A **will be available electronically via the SEC's website**. In addition, you also must complete Part 2B of Form ADV, which requires you to provide information about certain advisory personnel. Part 2B of Form ADV is not required to be filed electronically, and will not be publicly available on the SEC's website.

Form ADV should only be filed once you are ready to be fully compliant with the Advisers Act. It is the last step of the registration process.

assets held jointly with a spouse), calculated excluding the value of the person's primary residence and certain indebtedness (i.e., mortgages) secured by the residence; or (iii) is a "qualified purchaser" as defined in section 2(a)(51) of the Investment Company Act. Certain insiders are also considered qualified clients. Beginning in 2016, the SEC will adjust these dollar thresholds for inflation every five years.

Q: How long does it take to register?

Preparation for registration typically takes 3-6 months and may take significantly longer depending on the size of your business and the complexity of your operations. Generally speaking, when you file your Form ADV, the SEC checks to make sure that all appropriate questions have been answered and conducts a background check on all listed principals and owners. Going forward, the SEC may begin to undertake substantive review of Form ADV, paying specific attention to the disclosure in Part 2. Once you have filed your Form ADV, the SEC must approve your registration or begin proceedings to deny your registration within 45 days.

Q: How much does it cost to register?

Initial compliance costs vary greatly by adviser. For example, you may have already implemented policies and procedures for your business and operations, and find that you do not need to make many changes to become compliant with the Advisers Act. On the other hand, you may be starting from scratch, in which case you will likely incur development costs (such as attorneys fees) and implementation costs (such as costs associated with meeting email retention requirements and implementing disaster recovery program). Other incremental costs may also include the costs of hiring a new employee to act as Chief Compliance Officer.

Your IARD costs are limited to your initial set-up fee, which currently ranges from \$40 to \$225, based on your assets under management. There may also be an IARD processing fee, which is currently being waived.

You may also be subject to notice filing fees with certain states. These fees vary by state, and generally range from \$30 to \$500.

You will be subject to ongoing compliance costs once you register. The amount of such costs will vary substantially based on a variety of factors, such as the size of your business, the strategies you use and your existing infrastructure.

Q: If I register, do any of my affiliates also have to register?

Generally, fund managers may be able file a Form ADV that covers all of the entities in their organizational structure if the entities share the same employees and personnel and are subject to the same supervision and control. For example, if you have an entity that acts as investment manager to your funds and a separate entity that acts as general partner of the funds, and the general partner has the same personnel and follows the same policies and procedures as the investment manager, we would generally recommend that you file a single Form ADV that will serve to register both the investment manager and the general partner. Note that both the investment manager and the general partner will need to be operated as if they are registered and will be included in any SEC examination.

For larger complexes, an affiliate that is otherwise permitted to register may not wish to “piggyback” on a single registration and may choose to register separately for

marketing or other purposes. In any event, you should consult with your counsel as to your particular circumstances.

Q: What do I need to do after I register?

After you register, you will need to ensure that you continue to comply with the Advisers Act. For example, you will be required to: (i) annually update Part 1 and Part 2A of your Form ADV, and make interim updates and/or deliveries upon the occurrence of certain events; (ii) take certain actions with respect to accounts of which you have custody; and (iii) maintain required books and records. You will need to test your policies and procedures periodically (at least annually) to make sure they are effective and that you continue to be in compliance with the Advisers Act. You should develop a compliance calendar to monitor compliance responsibilities and deadlines.

In addition, you should review your offering documents, advisory agreements, counterparty agreements and other legal documents to determine if any revisions or other actions are necessary or advisable (to the extent that you have not already done so) and, at a minimum, let your clients and fund investors know that you are registered.

You should also start preparing for a routine SEC examination. One way to do so is to take a current SEC examination letter and prepare responses and gather documents and information to respond to the questions contained in the examination letter. We would be happy to provide you with a sample of a current SEC examination letter.

Q: What should I expect from a routine SEC examination?

In a routine examination, the SEC will typically send you a request for documents and information, and let you know when they will be visiting your office and interviewing your staff. Notice is typically given 2-3 weeks in advance (although there have been cases where no notice has been given). You should have a dedicated space for the SEC to work, where they can review documents and interview staff with minimal disruption to your business. Typically, the examination will last 8-10 business days on your premises. You should expect that the SEC will issue you a deficiency letter after completion of the examination, which will require that you respond with steps you are taking to remedy the deficiencies within 30 days.

Q: I am exempt from SEC registration, because I advise solely private funds and have regulatory assets under management of less than \$150 million or advise solely venture capital funds. Am I required to file anything with the SEC?

If you are not required to register with the SEC, because you are relying on the exemption for private fund advisers or for venture capital fund advisers (including if you are a foreign adviser relying on one of these exemptions), you are considered an “exempt reporting adviser” and are required to complete certain items in Part 1A of Form ADV and file the form with the SEC. Specifically, you are required to complete the questions in Part 1A of Form ADV relating to basic identifying information, the basis for your exemption from SEC registration, your form of organization, your other business

activities, your financial industry affiliations and private funds, your control persons and your disciplinary history.

You are also required to file updating amendments to your Form ADV at least annually, within 90 days of the end of your fiscal year, and more frequently, in certain circumstances.

If you are an exempt reporting adviser, you must complete and file your initial Form ADV no later than March 30, 2012.

Note that you are considered an “exempt reporting adviser” and you are make the filing discussed above even if you are registered with one or more states.

Q: Am I required to register with any individual states?

Once you are registered with the SEC, you are not required to register with any state. Individual states, however, may require certain notice filings. A state may also institute licensing, qualification or registration requirements for certain of your advisory personnel who have a place of business in that state. State rules vary considerably, and you should consult with your counsel as to your particular circumstances.

Guide to Registration

How To Register

Review and complete Form ADV Part 1 and Part 2

Form ADV has two parts: Part 1 and Part 2. Part 1 serves as the registration application with the SEC, and provides basic information about you and your associated persons. Part 1 requests general identifying information about your firm, information about your advisory business (including with regard to employees, clients, compensation, regulatory assets under management³ advisory activities and other business activities), financial industry affiliations, participation or interest in client transactions, custody, control persons and ownership and disciplinary history.⁴

Part 2 is intended primarily for clients (and fund investors) and, therefore, contains more detailed information regarding your business practices, fee arrangements, conflicts of interest and advisory personnel. Part 2 is divided into two parts: Part 2A and Part 2B, and requires you to provide clients with clearly written and meaningful disclosure, in plain English, about your business practices, conflicts of interest and advisory personnel.

Part 2A (the “Brochure”) requests information about a variety of topics relating to your business practices and conflicts of interest. The Brochure must include a discussion of your advisory business and the types of clients you have, a discussion of material changes to the Brochure since the last annual update, risk factors involved in your investment strategy and disclosure of certain legal or disciplinary events. You are required to specifically discuss the conflicts of interest created by some of your business practices and how you address these conflicts. The Brochure contains an appendix for specialized disclosure relating to wrap fee programs.

Part 2B (the “Brochure Supplement”) requests information about certain advisory personnel. For each “supervised person”⁵ who provides advisory services to a client,

³ The SEC requires that you determine your regulatory assets under management by calculating the value of the securities portfolios with respect to which you provide continuous and regular supervisory or management services. You are required to include in your regulatory assets under management: (i) proprietary assets; (ii) assets managed without receiving compensation; (iii) assets of foreign clients; and (iv) uncalled capital commitments. In addition, you are not permitted to subtract outstanding indebtedness (including leverage) and other accrued but unpaid liabilities, and must value assets at their market value, or fair value if market value is unavailable. You must calculate your regulatory assets under management within 90 days prior to the date of filing your Form ADV.

⁴ Part 1 of Form ADV is divided into two sub-parts: Part 1A, which must be completed by all investment advisers registering with either the SEC or any state, and Part 1B, which must be completed only by investment advisers registering with a state. Form ADV Part 1, among other things, requests certain specific information about fund clients, including basic organizational, operational and investment characteristics of the fund, the amount of assets held by the fund, the nature of certain investors in the fund and the fund’s service providers.

⁵ Your “supervised persons” include your officers, partners, directors (or other persons occupying a similar status or performing similar functions) or employees, or other persons who provide investment advice on your behalf and are subject to your supervision or control.

you must prepare a Brochure Supplement, disclosing, among other things: (i) his or her formal education and business background; (ii) certain legal or disciplinary events; (iii) other capacities in which he or she participates in any investment-related business; (iv) any compensation he or she receives based on the sales of securities or other investment products; (v) economic benefits he or she receives from someone other than a client for providing advisory services; and (vi) how you monitor the advice he or she provides, including the name, title and telephone number of his or her supervisor.

Because Form ADV calls for extensive disclosure regarding individual officers, directors, partners and other owners, you should consider circulating a questionnaire to such individuals to gather sufficient background information for use in completing the Form.

Entitlement and Filing Fees

To register, you must electronically file Form ADV Part 1 and Part 2A through the IARD, an electronic clearinghouse for investment adviser registration administered by FINRA. You must first request access to the IARD through FINRA's entitlement program by completing and submitting originally executed copies of the forms contained in the IARD entitlement packet, which can be found online at <http://www.iard.com/GetStarted.asp>. When completing your entitlement package, you must designate a Super Account Administrator ("SAA"). The SAA is primarily responsible for controlling who has access to your IARD account and, therefore, who can complete, update and file your Form ADV.⁶ It may take up to two weeks to receive the account number for the firm (called a "IARD number") and a user ID and password for the SAA, though typically it takes just a few days.

Once the IARD number has been received, you will want to pre-fund the account with your initial set-up fee, which is based on your assets under management (the initial set-up fee is currently \$150 if you have between \$25 and \$100 million under management and \$225 if you have over \$100 million under management). The set-up fee will be deducted from your account once the initial Form ADV filing is made. IARD will also automatically calculate and remit the amount of notice filing and similar fees that you will owe to the states for which you must make notice filings.

Completing and Filing Form ADV; Notice Filings

Once IARD access has been granted, Form ADV Part 1 can be filled out online and electronically submitted. To access the Form ADV online, go to the IARD website at <https://crd.finra.org/iad> and type in your user name and password. Once you have been taken to the next screen, select the "IARD Main" tab to be taken to the IARD site map, and at the site map, click on the ADV - New Filing hyperlink under the "Forms" heading. At this point, you can create and save an electronic copy of Form ADV Part 1. You will need to click each section of the navigation bar, type the appropriate

⁶ The SAA also controls your access to any other FINRA applications you use. The SAA will be required to review periodically all user accounts and certify on your behalf that all designated users should retain authorization. Given the scope of the SAA's responsibility, FINRA recommends that you designate a senior member of your management team to serve in that role.

information and click “save” after completing each section. After you have completed the Form ADV, you should run a completeness check to ensure that all required fields have been completed. Once you have passed the completeness check, you can print and/or submit the filing by selecting the appropriate hyperlinks. Should you need to retrieve a filing that has been started, but not completed, follow the same steps as above but select the ADV - Pending Filing hyperlink under the “Forms” heading. A Form ADV that has been started, but not filed, will remain pending for up to 120 days, after which it will be automatically deleted from the IARD system.

Your Brochure must be filed electronically with the SEC, and **will be publicly available on the SEC’s website**. Brochure Supplements are not required to be filed electronically, and **will not be publicly available on the SEC’s website**. You are, and will continue to be, required to provide prospective clients with a copy of Part 2 or a brochure containing at least the same required information, and to maintain a copy of Part 2 as part of your books and records. While the SEC has stated that a hedge fund or private equity fund manager’s clients are the funds themselves, and not the underlying fund investors, we nevertheless recommend that Part 2 be delivered to fund investors and prospective fund investors.

While states generally are preempted from requiring you to register with them once you are registered with the SEC, they are not prohibited from requiring you to pay certain fees and make notice filings of documents you file with the SEC. These requirements vary by state, but generally hinge on whether you have a place of business in the state or the number of clients you had over the past 12 months that are residents of that state. You may submit notice filings to the states through the IARD concurrently with your SEC registration application by checking the appropriate boxes in Form ADV Part 1 and pre-funding the fees required by the states at the same time you pay your initial set-up fee to FINRA.

Form ADV should only be filed once you are ready to be fully compliant with the Advisers Act. It is the last step of the registration process.

Obtaining SEC approval

Once you have submitted your Form ADV, the SEC has 45 days to approve your registration or to begin the process to determine whether your registration should be denied. Generally speaking, when you file your Form ADV, the SEC checks to make sure that all appropriate questions have been answered and conducts a background check on all listed principals and owners. Going forward, the SEC may begin to undertake substantive review of Form ADV, paying specific attention to the disclosure in Part 2. Assuming the SEC does not identify a deficiency in your Form ADV, the SEC will mail you an Effective Order once your registration is deemed effective. Alternatively, you may check your status on the IARD website. Once your registration is effective, Form ADV Part 1 and Part 2A **will be publicly available through the SEC’s website**.

SEC Registered Investment Adviser Requirements

SEC registered investment advisers are subject to a number of requirements and restrictions. **Because there is no grace period for compliance, you must be in full compliance with the provisions of the Advisers Act at the time your registration becomes effective.** Since approval typically occurs within 45 days after filing an initial Form ADV, you will need to begin taking steps needed to become compliant with the Advisers Act at least several months prior to filing the Form ADV. We recommend contacting counsel as soon as possible after determining that you will be registering as an investment adviser in order to have sufficient time to review your business and operations and put into place any necessary or appropriate policies, procedures and operational changes.

In addition, you will need to review your offering documents, advisory agreements, fund subscription agreements, marketing materials, counterparty agreements (including ISDAs) and other legal documents to assess whether any modifications need to be made, notices need to be given, consents need to be obtained and/or other actions need to be taken with regard to registration. You should also notify your clients and fund investors, including by indicating that you are a registered investment adviser in your fund offering documents. Note that if you are updating a fund's offering documents, you should review the offering documents in detail and in their entirety to determine if additional changes should be made. These materials will need to be prepared in advance so that they are ready as soon as your registration becomes effective.

Here are outlines of some of the key compliance requirements that apply to investment advisers registered with the SEC:

Compliance Infrastructure (Rule 206(4)-7)

- Development of Compliance Policies and Procedures

You are required to adopt and implement written policies and procedures reasonably designed to prevent violations of the Advisers Act and the rules thereunder by you or any of your supervised persons. While seemingly straightforward, the scope of this rule is extremely broad and the SEC has not provided much detailed guidance on structuring compliance policies and procedures. The SEC, however, has indicated that, at a minimum, these compliance policies and procedures should address the following topics (in addition to addressing compliance with the Advisers Act and its rules) to the extent relevant:

- Portfolio management processes, including allocation of investment opportunities among clients, consistency with client objectives and applicable regulatory restrictions;
- Trading practices, including procedures by which you satisfy your best execution obligation, use client brokerage to obtain research and other services (i.e., soft dollar arrangements) and allocate aggregated trades among clients;

- Proprietary trading and personal trading activities of supervised persons in a manner reasonably designed to prevent the misuse of material nonpublic information;
- Accuracy of disclosures made to fund investors, clients and regulators, including account statements and advertisements;
- Safeguarding of client assets from conversion or inappropriate use by advisory personnel;
- Accurate creation of required records and their maintenance in a manner that secures them from unauthorized alteration or use and protects them from untimely destruction (for a detailed description of required records, see “Recordkeeping Requirements” below);
- Marketing of advisory services, including the use of solicitors;
- Processes to value client holdings and assess fees based on those valuations, including ensuring that these processes are appropriate in view of the fact that you receive compensation based on those valuations; and
- Business continuity plans, including plans to address disaster recover and, for smaller firms, deaths of owners and/or key personnel.

If you already have written policies and procedures regarding the operation of your business, they should be reviewed to determine whether they reflect actual practices and also to identify any practices and/or gaps that need to be addressed prior to registration. This is especially important given the unprecedented degree of scrutiny of registered investment advisers by the SEC and other regulatory authorities in the wake of recent scandals, and related criticism of the SEC and other regulators for lacking the capacity to oversee those firms effectively.

There is no “one-size-fits-all” approach to creating, maintaining or enforcing policies and procedures, and any compliance policies and procedures should be tailored to your specific structure, investment strategy and operations. **You should not adopt an off-the-rack compliance manual.** Adopting generic compliance policies and procedures without undergoing a thorough review of operational practices might result in policies and procedures that are overly burdensome, impossible to implement or non-compliant with the rules. Compliance programs that appear ill-suited or ineffective may lead the SEC staff to conclude that compliance is not well-respected by you and that you are at high risk of violations. In such cases, the SEC staff is more likely to conclude that an in-depth review is necessary.

Any new or amended policies or procedures should be carefully reviewed by all affected personnel and should be tested prior to becoming effective. Ideally, this process should involve a committee comprised of senior management and appropriate business units, since the SEC staff has stated that management’s participation in this process will help to demonstrate a firm-wide commitment to compliance. Some policies or procedures might also require you to coordinate with outside service providers, including IT providers (e.g., for email retention and disaster recovery).

Several other rules under the Advisers Act mandate that you adopt written policies and procedures. We discuss these in more detail below.

- Appointment of Chief Compliance Officer

You must appoint a chief compliance officer (“CCO”) to be responsible for administering your compliance policies and procedures. The SEC has stated that a CCO should be competent and knowledgeable regarding the Advisers Act, have full responsibility and authority to develop and enforce appropriate policies and procedures and have sufficient seniority and authority to compel others to adhere to compliance policies and procedures. If you have not already designated a CCO, you will need to review the qualifications of your existing personnel in order to determine if anyone has the time and the expertise to handle the CCO responsibilities or if a CCO will need to be hired. We recommend that you commence this review and designate a CCO as soon as possible after the determination to register is made, so that your CCO can be actively involved in the development of your compliance policies and procedures from the outset.

The CCO should not automatically be placed in your legal department, which could lead to conflicts in the implementation and examination of the compliance program. The SEC staff has cautioned that, if the CCO reports through the general counsel, instances of client privilege must be clearly articulated and great effort must be made to segregate any dual responsibilities. The SEC takes the position that routine compliance monitoring is not subject to attorney-client privilege.⁷

- Ongoing Training

In order to encourage a culture of compliance in the work environment, you should institute training programs to promote better understanding of your compliance policies and procedures. Your fiduciary duties and obligations, avoiding potential conflicts of interest and the prevention of insider trading and employee harassment are just a few topics for training that you should consider.

- Annual Review

You are required to review the adequacy of your compliance policies and procedures and the effectiveness of their implementation on an annual basis,⁸ and you are encouraged to maintain written evidence of the review. Your annual review should consider matters that arose during the previous year that might require changes to your policies and procedures, including internal compliance matters, changes in your business activities and changes in the Advisers Act or other regulations.

⁷ Richards, Lori A., “The New Compliance Rule: An Opportunity for Change”. Investment Company Institute/Independent Directors Council, Mutual Fund Compliance Programs Conference, Washington, DC, June 28, 2004.

⁸ Note that you have 18 months after your policies and procedures are adopted or approved to complete the initial annual review.

You may also wish to conduct reviews more frequently than annually in light of similar matters that arise from time to time.

Other Policies and Procedures

- Code of Ethics (Rule 204A-1)

You are required to establish, maintain and enforce a written Code of Ethics that, at a minimum: (i) includes standards of business conduct that you require of your supervised persons; (ii) requires supervised persons to comply with applicable Federal securities laws; (iii) requires supervised persons to report any violations of the Code of Ethics to the CCO; and (iv) requires you to provide each supervised person with a copy of the Code of Ethics and any amendments, and obtain a written acknowledgement from the supervised person that he or she has received the Code of Ethics.

In addition, the Code of Ethics must require all “access persons”⁹ to report periodically, and for you to review, their personal securities transactions and holdings. Specifically, each access person must provide the CCO with a quarterly report of all of his or her personal securities transactions and an annual report listing his or her personal security holdings. You should also have provisions for pre-clearance of any investments in IPOs or private placements by access persons. For many fund managers, it is often appropriate that these requirements apply to all officers and employees, and not just access persons. You should also consider including other provisions that are not required, but nevertheless might be good business practices, such as restrictions on receiving gifts and preclearance of all personal securities transactions.

- Insider Trading (Section 204A)

You must establish, maintain and enforce written policies and procedures reasonably designed to prevent the misuse of material, non-public information by you or any person associated with you. The misuse of this information can include trading (either personally or on behalf of others) based on the information, or communicating the information to others (*i.e.*, “tipping”). While the scope of the rules against insider trading are not always clear, as a general rule of thumb you cannot use material, non-public information obtained from an issuer or another third party for client or personal trading. In addition, you cannot use material, non-public information about current or pending client investments (*e.g.*, actual or pending purchases and sales of securities), other than in connection with the investment of client accounts. To protect against such misuse, you may want to consider prohibiting your personnel from purchasing or selling securities that are under consideration for sale or purchase for client accounts or that have been sold or purchased recently for client accounts. Violations of the prohibition against insider trading may subject those involved to disciplinary action, as well as severe civil or criminal penalties.

⁹ An “access person” is any of your supervised persons who (i) has access to nonpublic information regarding any client’s purchase or sale of securities, or nonpublic information regarding the portfolio holdings of any reportable fund, or (ii) is involved in making securities recommendations to clients, or who has access to such recommendations that are nonpublic.

- Privacy Policy (Regulation S-P)

You are required to adopt policies and procedures that address administrative, technical and physical safeguards for the protection of customer records and information. In general, you are prohibited from providing non-public personal information about a customer or fund investor (such as a social security number or telephone number) to an unaffiliated third party, unless you have provided the customer or investor with an initial and an annual privacy notice describing, among other things, your policies and procedures for protecting this information. You must also give your customers and fund investors the ability to opt-out of having this information disclosed to unaffiliated third parties in some circumstances. While Regulation S-P only requires that these safeguards apply to clients and investors who are natural persons, we nevertheless recommend that you apply the same safeguards to entity clients and fund investors.

In addition, many states have specific rules and regulations on how you must treat the non-public personal information of their residents. State rules vary considerably, and you should consult with your counsel as to your particular circumstances.

- Proxy Voting (Rule 206(4)-6)

If you have voting authority over proxies for clients' securities, you are required to adopt and implement written policies and procedures that are reasonably designed to ensure that you vote proxies relating to portfolio securities in the best interests of clients. Note that you cannot merely state that you will vote proxies in the best interests of clients; rather, your policies and procedures should address how you will vote proxies, or what factors you will take into account when voting on particular matters. Your policies and procedures must also discuss how you address any conflicts of interest that are raised by your ability to vote proxies.

You must disclose information to clients about those policies and procedures, including how they may obtain information regarding how you voted their proxies. You must also furnish a copy of your proxy voting policies and procedures to clients upon request.

Updating and Delivering Form ADV (Rule 204-1)

- Part 1 of Form ADV

You are required to file an annual update of Part 1 of Form ADV through the IARD within 90 days after the end of your fiscal year. In addition, certain information contained in Part 1 must be amended promptly whenever it becomes inaccurate, and certain other information must be amended promptly whenever it becomes materially inaccurate (these items are set out in more detail in the instructions to Form ADV). The question of whether information is materially inaccurate is based on the particular facts and circumstances. Typically, no fees are charged for filing an amendment to Form ADV, except for an annual updating amendment.

- Part 2 of Form ADV

The Brochure will need to be updated annually and promptly when information (other than assets under management, the fee schedule or the summary of material changes) becomes materially inaccurate. In addition, the Brochure and each Brochure Supplement will need to be updated promptly when the adviser adds a disciplinary event or changes material information relating to a disciplinary event.

In general, a current Brochure must be delivered to clients before or at the time you enter into the advisory contract. A Brochure Supplement must initially be given to each client (including sophisticated clients) at or before the time when the applicable supervised person begins to provide advisory services to such client. In addition, within 120 days after the end of your fiscal year, you must deliver to clients an updated Brochure or a summary of material changes that includes an offer to provide a full copy of the Brochure. You must also deliver an updated Brochure and/or an updated Brochure Supplement (or a document summarizing the material facts) promptly whenever you add a disciplinary event or change material information relating to a disciplinary event.

Note that you are only required to deliver the Brochure and applicable Brochures Supplements to each of your “clients”. With respect to funds, your “client” is the fund. Accordingly, you are required to deliver the Brochure and applicable Brochure Supplements only to the fund, and not to fund investors. We strongly suggest, however, that you provide the Brochure and all applicable Brochure Supplements to your fund investors as well.

- Brochure Rule (Rule 204-3)

You are required to provide existing and prospective clients with a copy of Part 2 of Form ADV or a brochure containing at least the same information required in Part 2 in accordance with the timing above. We generally do not recommend that you develop a brochure that is separate from Part 2.

Recordkeeping Requirements (Rule 204-2)

In general, you are required to keep two categories of books and records: (i) typical business accounting records; and (ii) records related to your advisory business. Required records include, without limitation:

- Advisory business financials and accounting records, including cash receipts and disbursement journals, income and expense account ledgers, checkbooks, bank account statements, advisory business bills and financial statements;
- Records that pertain to providing investment advice and transactions in client accounts with respect to such advice, including orders to trade in client accounts, trade confirmation statements received from broker-dealers, documentation of proxy vote decisions, written requests for withdrawals or documentation of deposits received from clients and written correspondence

sent to or received from clients or potential clients discussing your recommendations or suggestions;

- Records that document your authority to conduct business in client accounts, including a list of accounts in which you have discretionary authority, documentation granting you discretionary authority and written agreements with clients, such as advisory contracts;
- Advertisements and performance records, including newsletters, articles and computational worksheets demonstrating performance returns;
- Records related to the Code of Ethics, including those addressing personal securities transaction reporting by access persons;
- Records regarding the maintenance and delivery of your written disclosure document (Brochures) and disclosure documents provided by certain solicitors who seek clients on your behalf; and
- Policies and procedures, including any documentation prepared in the course of your annual review.

You should also maintain executed copies of all of your organizational documents. You may be required to maintain additional records based on your specific operations (e.g., where you have custody or possession of a client's funds or securities).

Generally, most books and records must be kept for five (5) years. For the first two (2) of these years, records must be kept in your office; thereafter, such books and records must be kept in an easily accessible location. If you maintain any original books and records somewhere other than your principal office and place of business (such as with a fund's administrator), this must be noted on your Form ADV.

Original books and records may be stored using either micrographic or electronic media, and should generally be producible promptly (generally within 24 hours) upon request by the SEC staff. To ease this process, electronic records must be arranged and indexed in a way that permits easy location, access and retrieval. Note that you may store duplicate copies of your advisory records in a location separate from your principal office in order to ensure the continuity of business in the case of a disaster.

In addition to these books and records, the Dodd-Frank Act permits the SEC to adopt additional rules that will require you to maintain additional records relating to the hedge funds and/or private equity funds you advise.

Form PF (Rule 204(b)-1)

You are required to report certain information to the SEC on new Form PF, which the SEC will provide to the Financial Stability Oversight Council to allow it to monitor systemic risk. Form PF includes specific, detailed disclosure relating to your assets under management (including certain breakdowns thereof) and other fund-specific data. Information reported on Form PF is confidential, although the SEC and the CFTC may use Form PF information in examinations, enforcement actions and for investor protection. You are only required to complete and file Form PF if you have at least \$150

million of regulatory assets under management attributable to hedge funds, private equity funds and other private funds.

If you have at least \$5 billion of regulatory assets under management attributable to hedge funds, you must file Form PF quarterly, and your initial Form PF must be filed within 60 days after the first fiscal quarter end occurring after June 15, 2012, which for most advisers will be August 29, 2012, and within 60 days after each quarter end thereafter.

If you have less than \$5 billion but more than \$1.5 billion in regulatory assets under management attributable to hedge funds, you must file Form PF quarterly, and your initial Form PF must be filed within 60 days after the first fiscal quarter end occurring after December 15, 2012, which for most advisers will be March 1, 2013, and within 60 days after each quarter end thereafter.

If you have more than \$150 million but less than \$1.5 billion in regulatory assets under management attributable to hedge funds or you advise private equity funds, you are required to file Form PF annually, and your initial Form PF must be filed within 120 days after first fiscal year occurring after December 15, 2012, which for most advisers will be April 20, 2013, and within 120 days of the end of each fiscal year thereafter.

Form PF asks for a significant amount of detailed information, and you should budget significant time for completing the initial filing.

Performance-Based Fees (Rule 205-3)

You are permitted to charge a performance-based fee or allocation only to clients that are “qualified clients”. A qualified client is: (i) any person or entity that immediately after entering into the advisory contract has at least \$1,000,000 under management with you; (ii) any person or entity that you reasonably believe, immediately prior to entering into the advisory contract, either has a net worth (together, in the case of a natural person, with assets held jointly with a spouse) of more than \$2,000,000¹⁰ or is a “qualified purchaser” under the Investment Company Act at the time the contract is entered into; and (iii) certain of your executive officers, directors, trustees, general partners and other employees. [Note that, beginning in 2016, the SEC will adjust these dollar thresholds for inflation every five years.] Solely for purposes of this rule, you are required to look through each 3(c)(1) fund you advise and you are only permitted to charge a performance-based fee or allocation to an equity owner of the fund that is a qualified client. **Existing clients and fund investors are grandfathered for purposes of this rule, and these clients and fund investors can add to their existing investments even if they do not meet the qualified client test.**

¹⁰ For natural persons, this test is calculated excluding the value of the primary residence of such natural person and any indebtedness secured by the residence, but including indebtedness secured by the residence in excess of its estimated fair market value and any indebtedness incurred 60 days before the proposed investment date (unless such indebtedness is used to purchase the residence).

Note that you are not required to make a determination with respect to clients and fund investors that you know are qualified purchasers (including investors in any 3(c)(7) fund), since qualified purchasers automatically meet the definition of qualified clients.

You may need to amend your funds' subscription agreements to include a qualified client questionnaire. Note that you will not need to include a separate qualified client questionnaire in a subscription agreement for a 3(c)(7) fund (because each investor in a 3(c)(7) fund should complete a qualified purchaser questionnaire, and qualified purchasers automatically meet the definition of qualified clients).

Solicitation Arrangements (Rule 206(4)-3)

You must comply with certain requirements if you pay cash compensation to a solicitor for referring new clients to you. You should review your agreements with solicitors prior to registration and make appropriate changes to comply with the terms of this rule (you should also keep in mind the *Pay to Play* rule, which is discussed in item 10 below).

Generally, the payment must be made pursuant to a written agreement between you and the solicitor. Subject to certain limited exceptions, the written agreement must describe the solicitor's activities and compensation, contain the solicitor's undertaking to perform those duties under the agreement in a manner consistent with your instructions and the Advisers Act and require the solicitor, at the time of any solicitation, to provide the client with a copy of your brochure (generally Part 2 of your Form ADV) and a separate written disclosure document.

This separate disclosure document must contain: (i) your name and the name of the solicitor; (ii) the nature of your relationship with the solicitor; (iii) a statement that you will compensate the solicitor for his or her solicitation services and the terms of the arrangement; (iv) the amount, if any, that will be charged to the client in addition to the advisory fee for solicitation services; and (v) the differential, if any, among clients with respect to the amount or level of advisory fees you charge if such differential is due to the solicitation arrangement. You must receive a signed and dated acknowledgement showing that the client received the separate written disclosure document. You also must make a bona fide effort to ascertain that the solicitor has complied with the terms of your agreement, and you must have a reasonable basis for believing that the solicitor has so complied.

In addition, a cash referral fee may not be paid to any solicitor who: (i) is subject to an SEC order under Section 203(f) of the Advisers Act; (ii) was convicted of any felony or misdemeanor within the past ten years involving the purchase or sale of any security, the taking of a false oath, the making of a false report, bribery, perjury, burglary or any substantially equivalent activity, or conspiracy to commit any such offense; (iii) was found by the SEC to have (a) made, or caused to be made, a false or misleading statement in any application for registration or report to be filed under the Advisers Act, (b) willfully violated any provision of the Securities Act, the Exchange Act, the Investment Company Act, the Advisers Act, the Commodity Exchange Act or certain other rules and regulations, or (c) willfully aided or abetted the violation by any other

person of these laws, rules and regulations, or has failed to reasonably supervise another person who commits such violation, if such other person is subject to his or her supervision; or (iv) is enjoined from acting as an investment adviser, broker-dealer or in certain other capacities. This is generally called the “Bad-Boy Rule”.

Note that the provisions of this rule do not apply to the payment of a cash fee to compensate a person that solely solicits investors to invest in a fund. Payment to persons that solicit investors to invest in separately managed accounts and funds, however, are subject to this rule.

In addition, please note that, even if a solicitation agreement is in compliance with this rule, a solicitor typically falls under the definition of a broker under the Exchange Act and various state laws (*i.e.*, generally any person engaged in the business of effecting transactions in securities for the account of others), and, if so, would need to be registered, or exempt from registration, as a broker-dealer.

Custody (206(4)-2)

If you have custody of clients’ funds or securities, you are required to maintain certain safeguards meant to protect these assets. “Custody” includes holding, directly or indirectly, client funds or securities, or having the authority to obtain possession of them (*i.e.*, by deducting advisory fees or withdrawing funds on behalf of a client). In addition, you have custody of a client’s assets where, by acting in a certain capacity (such as a general partner of a limited partnership or a manager of a limited liability company), you or one of your supervised persons has the authority to transfer assets in the account to itself. Further, you have custody of any client assets that are directly or indirectly held by a “related person”¹¹ in connection with the advisory services you provide. This rule applies if you have custody of the assets of a fund you advise.

In addition, the Dodd-Frank Act added Section 223 to the Advisers Act, which requires you to take such steps to safeguard client assets over which you have custody as the SEC may, by rule, prescribe. The SEC has not yet adopted any rules under this section.

- **Qualified Custodian**

If you have custody of client assets, you are generally required to place the assets with a qualified custodian (which includes, among others, banks and registered broker-dealers). The qualified custodian must maintain the assets in a separate account for each client (in that client’s name) or in accounts that contain only client assets. Shares of open-end mutual funds and privately offered securities are generally not required to be kept with a qualified custodian.

Once the custodial account is established on behalf of the client, you must provide details regarding the custodial arrangement to the client in a notice. Promptly upon opening a custodial account on a client’s behalf, and following any changes to the

¹¹ A “related person” is a person directly or indirectly controlling or controlled by you or a person under common control with you.

custodial account information, you must notify the client of the custodian’s name, address and manner in which the assets are maintained.

- Account Statements and Annual Surprise Examination

You are required to conduct a “due inquiry” in order to establish a reasonable basis for believing that the qualified custodian sends account statements to each client no less frequently than quarterly. Note that you cannot satisfy this provision of the rule by sending account statements yourself directly to clients. However, if you do send your own account statements to clients, the statement must urge clients to compare the account statements received from the custodian with the statements you send (note that this legend must also be included in any notice that you send to the client when the custodial account is opened).

In addition, you are required to undergo an annual surprise examination by an independent public accountant to verify client assets. The examination must be at a time that is irregular from year to year, and the accountant conducting the examination is required to submit certain information to the SEC. If you or a “related person” serves as the qualified custodian, then the annual surprise examination must be conducted by an accountant that is registered with and subject to regular inspection by the PCAOB (a “PCAOB Accountant”). The first examination must generally occur within six months of your registration.

You are not required to undergo an annual surprise examination if: (i) you are deemed to have custody of client assets solely as a result of a related person having custody of such assets; and (ii) you are “operationally independent” (as defined in the rule) from the related person. In addition, you are exempt from the examination requirement if you are deemed to have custody solely as a result of having authority to withdraw advisory fees from client accounts.

With respect to a fund you manage, you are exempt from these requirements if the fund is audited annually by a PCAOB Accountant and the fund sends copies of the audited financial statements to investors within 120 days of the end of the fund’s fiscal year (180 days for funds of funds).¹² If a fund does not timely distribute audited financial statements to its investors, then you must meet the requirements above (including by ensuring that account statements are sent to funds investors at least quarterly), and the fund’s privately offered securities must be maintained at a qualified custodian.

- Internal Control Report

If you or a related person serves as the qualified custodian of client assets (including fund assets), then you must obtain (or receive from your related person) a written report from a PCAOB Accountant with respect to your or your related person’s custody controls of client assets, including an opinion from the PCAOB Accountant (for example, a “Type II SAS 70 Report”). The internal control report must be obtained no

¹² You must also procure an audit upon liquidation of the fund and distribute audited financial statements to investors promptly upon completion of the liquidation audit.

less frequently than once each calendar year, and must be obtained even if you and the related person are operationally independent.

Advertising (Rule 206(4)-1)

You are required to ensure that your advertisements are not false or misleading and do not contain any untrue statement of a material fact. Specifically, you are prohibited from using advertisements that contain testimonials, cherry-pick past specific recommendations that were profitable, represent that any graph, chart or formula can, in and of itself, be used to determine which securities to buy or sell or state that any report, analysis or service is free, unless it really is free. You are also prohibited from attaching phrases such as “RIA” or “Registered Investment Adviser” to your name in a manner that implies that you: (i) are or have been officially endorsed, sponsored, recommended or approved by the SEC or any other governmental authority; or (ii) have specific professional competence, education or other special training.

Advertisements generally include your pitchbooks and marketing decks, and other communications addressed to more than one person that offer investment advisory services. Advertisements, however, generally do not include: (i) written communications responding to an unsolicited request by a client, prospective client or consultant for specific information about your past specific recommendations; and (ii) specific written communications to existing clients discussing your past specific recommendations concerning securities that are or were recently held by such clients, provided that the communication does not offer advisory services. You should review all of your advertisements prior to registering to ensure that they comply with the terms of this rule.

- **Advertising Performance**

Advertisements that contain performance information must, among other things: (i) disclose the effect of material market or economic conditions on the performance results; (ii) disclose whether and to what extent the results portrayed reflect the reinvestment of earnings; (iii) if results are presented in comparison to an index, disclose all material facts relevant to the comparison; and (iv) disclose any material conditions, objectives or investment strategies used to obtain the results. Your advertisements cannot suggest or make claims about the potential for profit without also disclosing the possibility of loss. Additional requirements must be met if you are presenting model performance results, including a prominent discussion of the limitations inherent in model results.

As a general rule, you must always present performance results net of fees and other expenses. You may, however, present gross performance results in private one-on-one presentations to wealthy investors if you provide certain additional information in writing, or if net performance results are presented with equal prominence as the gross performance results and in a format designed to facilitate ease of comparison.

- Testimonials Performance

You are prohibited from using an advertisement that contains testimonials. Testimonials include any statement by a former or present client that endorses you or refers to the client’s favorable investment experience with you. This prohibition is interpreted broadly.

You, however, may include a partial client list in your advertising materials, provided that: (i) you do not use performance-based data to determine which clients to include on the list; (ii) each list includes a prominent disclaimer that “it is not known whether the listed clients approve or disapprove of the adviser or the advisory services provided”; (iii) each list includes disclosure about the objective criteria used to determine which clients to include on the list; and (iv) each client identified on the list has consented to being identified. In addition, you may include in an advertisement a bona fide, unbiased third party report or article that meets certain conditions.

Pay to Play (Rule 206(4)-5)¹³

- Two-Year Time Out

You are prohibited from receiving compensation (directly or through an investment in a fund) from a “government entity” for two years after you or any of your “covered associates” makes a political “contribution” to an “official” of the government entity. You may, however, continue to provide advisory services to the government entity on a no-fee basis. This provision covers 3(c)(1) funds, 3(c)(7) funds and registered investment companies that are an investment option of a plan or program of a government entity.

- The term “official” is generally any person that is an incumbent, candidate or successful candidate for elective office who can, directly or indirectly, influence your being hired by the government entity. It does not include any of your covered associates.
- The term “government entity” is limited to state and local entities. These entities are typically pension plans that are separate legal entities from state and local governments, but have elected officials as board members.
- The term “covered associate” generally includes your executive officers, employees who solicit government entities (and their supervisors) and any PAC controlled by you or any of your covered associates.
- The term “contribution” includes anything of value made for the purpose of influencing an election, including any payments for debts incurred or payment of transition or inaugural expenses. The “time-out” could be triggered by a contribution to a PAC or political party that is intended to support a limited

¹³ Compliance with this rule generally was required by March 14, 2011, except that compliance with the prohibition on the use of third-party solicitors and certain provisions relating to certain registered investment companies (and related recordkeeping requirements) is required by June 13, 2012.

number of government officials. Contributions do not generally include independent expenditures made to express support for candidates, volunteering, making speeches or making charitable contributions.

The rule includes certain exceptions for de minimis contributions made by individual employees, generally in an amount up to \$350 per official (per election) for whom an employee is entitled to vote and up to \$150 per official (per election) for whom an employee is not entitled to vote. There is also an exception for a limited number of de minimis contributions that are discovered and returned within a certain time period.

When a person becomes a covered associate (including when an existing employee is transferred or promoted), you must “look back” in time to that person’s prior contributions to determine whether the “time-out” provisions of the rule apply. If the person is involved in soliciting clients, then you must look back two years. If the person is not involved in soliciting clients, then you are only required to look back six months.

We suggest circulating a questionnaire to all covered associates at least annually to determine what, if any, political contributions have been made. The same questionnaire should be completed by prospective employees that will become covered associates, and existing employees that are expected to become covered associates, to ensure compliance with the look-back provisions of this rule. In addition, since you may become aware of the political affiliations of your covered associates in the course of administering these questionnaires, you should have procedures in place and possibly also take additional precautions designed to ensure that employment related decisions, including the decision to hire or fire any employee, are not made on the basis of political affiliation as well as implementing measures to prevent other forms of workplace discrimination.

Further, so you are not required to manage the assets of a governmental entity without receiving compensation, you may wish to provide in your fund documents and other client agreements that you can terminate the relationship with the government entity for any reason at any time.

- Soliciting Contributions and Payments

You and your covered associates are prohibited from soliciting or coordinating: (i) contributions to an official of a government entity to which you are seeking to provide investment advisory services; or (ii) “payments” (as defined in the rule) to a political party of a state or locality where you are providing or seeking to provide investment advisory services to a government entity.

For example, if you are providing or seeking to provide investment advisory services to a government entity, you are prohibited from: (i) indirectly making political contributions to an official of the government entity through spouses, lawyers or affiliated companies; (ii) soliciting contributions from professional service providers; (iii) “bundling” a large number of small employee contributions to influence an election in the relevant state or locality; (iv) consenting to the use of your name on

fundraising literature; and (v) sponsoring a meeting or conference that features an official as an attendee or guest speaker and involves fundraising for the official.

For the purposes of this rule, responding to a request for proposal, communicating with a government entity regarding that entity's formal selection process for investment advisers or engaging in some other solicitation of investment advisory business of the government entity will be deemed seeking to provide advisory services to a government entity.

- **Prohibition on Third Party Solicitation**

You and your covered associates are prohibited from paying any person to solicit a government entity, unless such person is: (i) a "regulated person" (i.e., a registered investment adviser, registered municipal adviser or registered broker-dealer) that is subject to prohibitions against engaging in pay-to-play practices; or (ii) one of your employees, general partners, managing members or executive officers (although contributions by these persons may trigger the two-year time out). You should review your current third-party solicitors to make sure they are able to perform services for you under this rule.

The prohibition does not extend to payments by you to non-affiliated persons that provide you with legal, accounting or other professional services in connection with specific investment advisory business, as long as such persons are not being paid by you (directly or indirectly) for communicating with the government entity for the purpose of obtaining or retaining investment advisory business for you.

- **Recordkeeping**

If you provide investment advisory services to government entities, you must make and keep a record of all political contributions made by you and your covered associates in the past five years (but not prior to September 13, 2010). You must make and keep records that include: (i) the names, titles and business and home addresses of all covered associates; (ii) all government entities to which you provide or have provided investment advisory services, or which are or were investors in any fund to which you provide or have provided investment advisory services, in the past five years (but not prior to September 13, 2010); (iii) all direct or indirect contributions made by you or any of your covered associates to an official of a government entity, or direct or indirect payments to a political party of a state or political subdivision thereof, or to a PAC; and (iv) the name and business address of each regulated person to whom you provide or agree to provide, directly or indirectly, payment to solicit a government entity for investment advisory services.

Advisory Contracts (Section 205)

Your advisory contracts with clients must meet certain requirements. Specifically, each advisory contract must provide that it may not be assigned by you to any other person without the prior consent of the client. In addition, if your firm is a partnership, the contracts must provide that you "will notify the other party to the contract of any

change in the membership of such partnership within a reasonable time after such change”.

Anti-Fraud (Rule 206(4)-8)

You are prohibited from: (i) making untrue statements of material fact, or omitting to state a material fact necessary to make the statements made not misleading, to any fund investor or prospective fund investor; or (ii) engaging in any act, practice or course of business that is fraudulent, deceptive or manipulative with respect to any fund investor or prospective fund investor. The SEC has indicated that the standard for enforcement of the anti-fraud rules will be a negligence standard and will not require intent or knowledge of wrongdoing on your part.

Accordingly, you should review your funds’ offering documents and all marketing materials for false or misleading statements or information, including biographical information and experience of management, information on and valuation of past returns and policies regarding disclosure to some groups of fund investors. For example, if you enter into a side letter with a fund investor that requires that you make certain disclosures, your failure to make these disclosures could raise issues under this rule.

SEC Examinations (Section 204)

Your books and records are subject to examination by the SEC staff. The main purpose of these examinations is to determine whether you are complying with federal securities laws, adhering to the disclosures you have provided to your clients and maintaining appropriate compliance programs to ensure compliance with federal securities laws. The examinations also provide the SEC and its staff with information about the effectiveness of securities rules and laws and the securities industry’s compliance efforts.

In general, there are three types of examinations: (i) routine examinations, where you are selected for examination based on risk- or time-based criteria or randomly (although there have been indications that the SEC will begin to rely more on tips, complaints and referrals in selecting investment advisers for routine examinations); (ii) “for cause” examinations, where information suggests that you might have been involved in a violation of the federal securities laws; and (iii) “sweep” examinations, where several advisers are simultaneously examined to investigate particular industry practices, with select follow-up examinations.

Notice of inspection is typically given anywhere from a few days to a few weeks in advance. The staff may arrive unannounced (without notice) when conducting for-cause examinations, an adviser’s first examination, an examination of a sales office or certain focused examinations. Exams typically include the SEC visiting your office and interviewing your staff. You should have a dedicated space for the SEC to work, where they can review documents and interview staff with minimal disruption of your business. Please keep in mind, however, that you should provide a secluded part of your office that provides adequate space for the SEC to perform its duties.

Exams are preceded or accompanied by a letter outlining the books and records to be produced for review by examiners on or by a specified date. The request for documents may be extensive.

In conducting its examinations, the SEC staff typically looks for the “output” of your policies and procedures. For example, if your procedures require that an internal committee meet quarterly to review your brokerage transactions for compliance with your soft dollar policies, the SEC staff will likely request to review the minutes of these meetings. The SEC staff has gone so far as to say that the SEC would prefer to see how you identify and resolve a breach of your policies and procedures, rather than to see that you have not identified any breaches at all.

While the duration of the examination depends on the size of your business and the scope of the examination, examinations typically average between eight to ten business days on your premises, with a view towards completion within 90 days. At the conclusion of its examination work, the staff will generally provide you with a preview of its conclusions. This may occur in person or, on occasion, by telephone. Sometimes these previews result in opportunities to correct misunderstandings by the staff. If, as occurs in most examinations, the staff identifies an issue, it will be noted in a deficiency letter to which you are requested to respond generally within 30 days. Responses should include the corrective measures, if any, you have taken in response to the deficiency. The response to requests and the attitudes of your personnel may affect the staff’s assessment of whether you have a “culture of compliance” and the strength of your compliance regime. Deficiencies discovered during the exam generally will be the first items reviewed on subsequent exams. Where significant violations are addressed through a deficiency letter, you should expect a follow-up inspection within one year.

State Requirements

General Discussion of State Requirements Applicable to Investment Advisers

If you are registered with the SEC or excepted from the definition of investment adviser, a state can only require you to make a notice filing and pay certain fees if you have one or more clients or otherwise do business in that state. The National Securities Markets Improvement Act (commonly referred to as NSMIA), generally preempts states from requiring the registration, licensing or qualification of an investment adviser or any of its supervised persons if the investment adviser is registered with the SEC as an investment adviser or if it is a person or entity that is excepted from the definition of investment adviser under the Advisers Act.

States generally require notice filings to be made through the IARD and the filing that is typically required is Part 1 of your Form ADV. Most states also require you to file Part 2 of your Form ADV through the IARD.

If you are not registered with the SEC as an investment adviser or excepted from the definition of investment adviser, a state may require you to register or be licensed or otherwise qualified only if: (i) you have a “place of business” located in that state; or

(ii) you have more than 5 clients that are residents of that state during the preceding 12-month period. A place of business is an office at which you (or your representatives) regularly provide or hold yourself out to the public as providing investment advisory services, or at which you solicit, meet with or otherwise communicate with clients. To determine the number of clients, you generally may treat a fund as a single client and not count the individual fund investors towards the threshold. Therefore, if you are not registered with the SEC as an investment adviser (or excepted from the definition of investment adviser) and have no place of business in a state and advise only 5 or fewer funds, you would not be required to register with that state whether or not more than 5 persons have invested in the fund.

If you are exempt from SEC registration because you advise solely hedge funds and/or private equity funds and have regulatory assets under management of less than \$150 million, are a foreign private adviser or because you advise solely venture capital funds, you must consider whether you are subject to regulation in any states in which you do business, including those states in which a fund you manage has made sales of its securities, states in which you (or a person authorized by you) solicit investors and states in which you have employees. Certain states may provide exemptions from registration for advisers who provide advice only to institutional clients or advisers that are exempt from registration with the SEC. State rules vary considerably, and you should consult with counsel as to your particular circumstances.

General Discussion of State Requirements Applicable to Investment Adviser Representatives

In addition to determining the extent to which state regulations are applicable to you, you must also consider whether your supervised persons are subject to regulation by a state. NSMIA preempts state laws requiring the registration, licensing or qualification of your supervised persons if you are registered with the SEC or excepted from the definition of investment adviser, except that a state may license, register or otherwise qualify any of your “investment adviser representatives” (as defined below) who has a place of business in that state.

If you are not registered with the SEC or excluded from the definition of investment adviser, then you must consider whether your employees, agents or other persons engaging in activities on your behalf are required to be registered, licensed or qualified with a particular state. In such case, we recommend that you consult the laws of each state in which you do business, including those states in which a fund you manage has made sales of its securities, states in which you or someone working on your behalf solicits investors and states in which you have employees.

The laws of the states differ with respect to whether your employees, agents or other persons engaging in activities on your behalf are required to be registered, licensed or qualified. Some states use the Advisers Act’s definition of “investment adviser representative” to determine who must be registered, licensed or qualified, but others do not. Generally speaking, however, many require the registration, licensing or qualification of a person who, for compensation: (i) makes any recommendations or

otherwise renders advice regarding securities; (ii) manages accounts or portfolios of clients; (iii) determines which recommendation or advice regarding securities should be given; (iv) solicits, offers, or negotiates for the sale of or sells investment advisory services; or (v) supervises employees who perform any of the foregoing.

- General Requirements Regarding Investment Adviser Representatives

As mentioned above, if you are registered with the SEC or excepted from the definition of investment adviser, a state may license, register or otherwise qualify any of your “investment adviser representatives” who have a place of business in that state. An “investment adviser representative” is defined as a “supervised person” (i) who has more than 5 clients who are natural persons (other than “excepted persons”¹⁴) and (ii) more than 10% of whose clients are natural persons (other than “excepted persons”). If any of your supervised persons meet the definition of investment adviser representative in a state in which he or she has a place of business, such state may license, register or otherwise qualify him or her. If, however, a person does not on a regular basis solicit, meet with or otherwise communicate with your clients (or only provides “impersonal investment advice”¹⁵), he or she will generally not be considered to be an “investment adviser representative”. As a result, your personnel who are involved in formulating investment advice for your clients, but not directly involved in providing the advice or soliciting clients, generally are not considered to be “investment adviser representatives” and are excluded from state regulatory requirements.

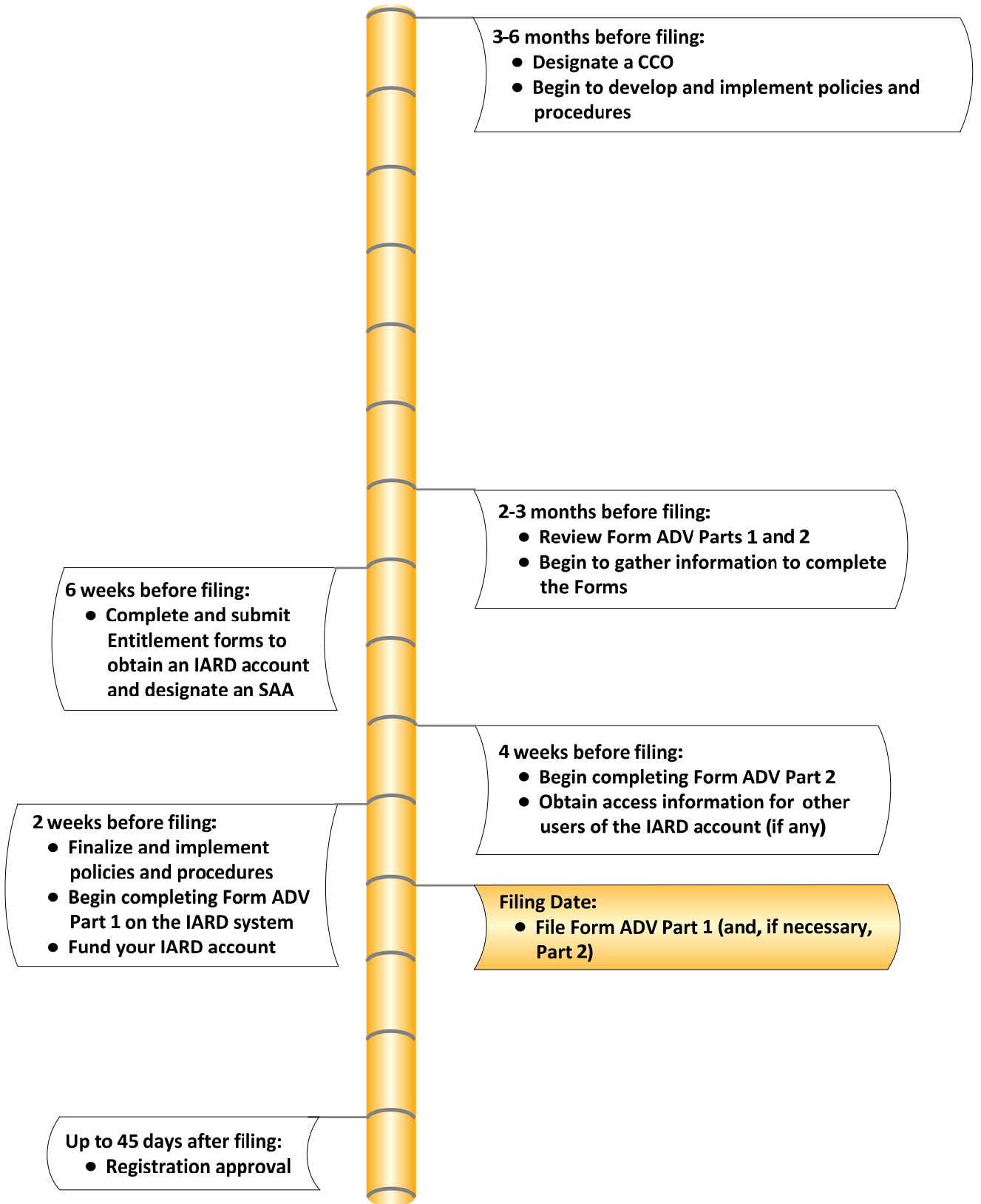
Practically speaking, if you advise only funds, you would not have any investment adviser representatives, since funds are not natural persons. If you also manage separate or managed accounts, however, you may have “investment adviser representatives”.

Registration of investment adviser representatives is frequently completed via filing a Form U-4 and paying a fee through IARD. In addition, most states require investment adviser representatives to pass exams, such as either a Series 66 and Series 7 or Series 65, although many states exempt investment adviser representatives who have received certain industry certifications, such as certified financial planner, chartered financial analyst, chartered financial consultant and others.

¹⁴ An “excepted person” is a client who is a natural person and (a) has at least \$1,000,000 under the adviser’s management, (b) has a net worth (together with his or her spouse) of more than \$2,000,000, (c) is an executive officer, director, trustee or general partner of the adviser, (d) is an employee of the adviser who participates in the investment activities of the adviser as part of his or her regular functions or duties and has been performing such duties or functions for the adviser or another adviser for at least 12 months, or (e) has (together with his or her spouse) at least \$5 million in investments. Persons soliciting clients for investment advisers are also governed by these definitions.

¹⁵ “Impersonal investment advice” means investment advisory services provided by means of written material or oral statements that do not purport to meet the objectives or needs of specific individuals or accounts.

TIMELINE FOR SEC REGISTRATION



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