

Morgan Lewis

**2010 ANNUAL PRIVATE FUND
INVESTORS ROUNDTABLE**
an essential business, legal and regulatory discussion

Regulatory Initiatives
Overview of U.S. Regulatory Reform

Jennifer Klass

U.S. Regulatory Reform

- Currently two Bills in the legislative pipeline:
 - “Wall Street Reform and Consumer Protection Act of 2009” (H.R. 4173)
 - *Passed by House 12/11/2009*
 - “Restoring American Financial Stability Act of 2010” (Dodd Bill)
 - *Approved by Senate by Banking Committee 3/22/2010*
- Both HR 4173 and Dodd Bill contain versions of the “Private Fund Investment Advisers Registration Act”

U.S. Regulatory Reform (cont.)

- Private Fund Investment Advisers Registration Act of 2010 (Dodd Bill)
 - All advisers to “private funds” must register, subject to certain exceptions
 - “Private fund” is any issuer that relies on Section 3(c)(1) or 3(c)(7)
 - Eliminates Section 203(b)(3) exemption for fewer than 15 clients
 - Raises threshold for SEC registration from \$25 to \$100 million

U.S. Regulatory Reform (cont.)

- Advisers Act registration not required for:
 - Advisers to “venture capital funds”
 - Advisers to “private equity funds”
 - *Required to maintain records and provide SEC with reporting based on fund size, governance, investment strategy, risk and other factors*
 - “Foreign Private (Fund) Advisers”
 - *No place of business in U.S.*
 - *Fewer than 15 U.S. clients*
 - *Less than \$25 million in AUM from U.S. clients and investors*
 - *Does not hold itself out in U.S.*
 - *Does not act as investment adviser to a registered investment company or business development company*
 - Advisers solely to “small business investment companies”

U.S. Regulatory Reform (cont.)

- **Books and Records**
 - SEC has authority to require registered advisers to maintain records and provide reports regarding private funds
 - Records and reports may be provided to Financial Stability Oversight Council (systematic risk)
 - Records and reports of private funds are considered books and records of the adviser
- **Collection of Systematic Risk Data**
 - Amount of AUM and use of leverage
 - Counterparty credit risk exposure
 - Trading and investment positions
 - Valuation policies and practices of fund
 - Type of assets held
 - Side letters or arrangements
 - Trading practices
 - Other information as SEC, in consultation with the Council, determines necessary or appropriate for the protection of investors or for the assessment of systematic risk

U.S. Regulatory Reform (cont.)

- Examination of Records
 - Extends SEC examination authority to all records relating to private funds
- Data Collection and Confidentiality
 - Information sharing between SEC and Council
 - Confidentiality of information received by SEC and Council, as well as other recipients
 - Protection of proprietary information (e.g., trading strategies, research methodologies, trading data, hardware or software containing intellectual property)
- Arbitration of Disputes
- Delegation of Custody to SEC Rules

U.S. Regulatory Reform – Volcker Rule

- Restrictions on capital market activity by banks and bank holding companies
 - Authorizes Federal banking agencies to prohibit insured depository institutions, entities that control insured depository institutions (including bank holding companies) and any subsidiaries from
 - *Engaging in “proprietary trading;” or*
 - *Sponsoring or investing in a hedge fund or private equity fund*
- Proprietary trading does not include trading on behalf of a customer, as part of market making activities, or otherwise in connection with or in facilitation of customer relationships, including risk-mitigating hedging activities
- Sponsoring extends to corporate control, controlling directors, trustees or management of fund, sharing same name
- Limitations on affiliated transactions and capital requirements
- Council study and rulemaking required to implement