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## Dodd-Frank Act Rulemaking - SEC Issues Order Adjusting Dollar Amount Thresholds For Qualified Client Rule Under the Advisers Act

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On July 12, 2011, the Securities and Exchange Commission (the "SEC") issued an order adjusting the dollar amount thresholds set forth in the assets under management and net worth tests in the *qualified client* rule to \$1,000,000, with respect to the assets under management test, and \$2,000,000, with respect to the net worth test. As described in the Lowenstein Sandler PC Client Alert available [here](#), registered investment advisers are generally prohibited from collecting any performance-based compensation, subject to certain exceptions including pursuant to the *qualified client* rule set forth in Rule 205-3 under the Investment Advisers Act of 1940, as amended. The SEC's order was issued in furtherance of a May 10, 2011 SEC-proposed rule release, and is part of the SEC's continued rulemaking initiative under the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010.

As discussed in more detail in Lowenstein Sandler PC's Client Alert, referenced above, the SEC's May 10th proposed rule release had also proposed to (i) exclude the value of a person's primary residence from the determination of whether or not a person meets the requisite net worth standards under the *qualified client* rule; (ii) allow for certain transition provisions (i.e., a "grandfathering" provision specifying that (A) the revised thresholds would apply only to new contractual arrangements; (B) additional investments by any clients/investors who were parties to such existing contractual arrangements would be permitted; and (C) any investment adviser previously exempt from registration pursuant to Section 203 of the Advisers Act would not be subject to the revised thresholds with respect to contractual arrangements entered into when exempt from registration); and (iii) establish a method for future adjustments to the dollar amount tests in the *qualified client* rule. The SEC's July 12th order does not implement these proposals but does specify that the SEC intends to evaluate public comments that it has received before determining whether such proposals will be adopted. As a result, while new clients/investors will be subject to the revised thresholds after the effective date of the SEC's order (noted below), the market is awaiting further SEC guidance relating to the treatment of current performance-based compensation arrangements. We expect that some form of "grandfathering" provision will be given effect, but there are no guarantees or related details until the SEC formally adopts as much.

The SEC's order will require registered investment advisers to review and revise, as necessary, offering memoranda and subscription documents for private investment funds that rely upon the Section 3(c)(1) exemption under the Investment Company Act (i.e., those private investment funds with not more than 100 investors). Private investment funds that rely upon the Section 3(c)(7) exemption under the Investment Company Act (i.e., those private investment funds with only *qualified purchaser* investors) are not subject to the restrictions discussed in this Client Alert. Registered investment advisers will also be required to address

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the revised thresholds with respect to any future managed account agreements. Lowenstein Sandler's Investment Management Group encourages investment advisers to review their current advisory documentation and to consider what actions may be required in light of the SEC's order.

The SEC's order, which may be found [here](#), is effective as of September 19, 2011.

Lowenstein Sandler's Investment Management Group will keep you informed of any final further developments relating to the SEC's May 10th rule proposal.

In the interim, please contact any of the attorneys listed, or any other member of [Lowenstein Sandler's Investment Management Group](#), for further information on the matters discussed in this summary.

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