Warshaw Burstein Cohen Schlesinger & Kuh, LLP

M E M O R A N D U M

To: Our Clients and Friends **Date:** August 27, 2009

From: Warshaw Burstein Cohen Schlesinger & Kuh, LLP

RE: Pending Proposals Impacting the Investment Management Industry – Mid-Year Update

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Numerous items of legislation impacting the investment management industry, including hedge funds, private equity funds and their advisers, are now pending in Congress. In addition, the Securities and Exchange Commission has proposed two rules under the Investment Advisers Act of 1940 (the "**Advisers Act**"). Below is a brief summary of the key current proposals.

Proposals Regarding Registration of Investment Advisers. Three bills have been introduced this year that would alter the provisions of the Advisers Act governing the registration of investment advisers. The first, the Hedge Fund Adviser Registration Act of 2009, introduced by Representatives Capuano and Castle on January 27, would strike Section 203(b)(3) of the Advisers Act. This is the provision that exempts from registration under the Advisers Act those investment advisers that have fewer than 15 clients and do not hold themselves out to the public as investment advisers.

Both the Private Fund Transparency Act of 2009, which was introduced by Senator Reed on June 16, and the Private Fund Investment Adviser Registration Act of 2009, which was submitted to Congress by the Treasury Department on July 15, 2009, take a different approach. Both Acts also would eliminate the current Section 203(b)(3) of the Advisers Act, however, each would replace it with an exemption for foreign private advisers. Both Acts define a foreign private investor as one that (i) does not have a US place of business, (ii) has had fewer than 15 clients in the US during the preceding 12 months; (iii) has less than $25 million in assets under management that attributable to US clients; (iv) does not hold itself out to the US public as an investment adviser, and (v) does not serve as an investment adviser to a registered fund or a business development company. In addition, both proposed Acts also would require registered investment advisers to maintain records and submit reports to the extent "necessary or appropriate in the public interest" for purposes of assessing systemic risk. While Senator Reed's proposal does not specify any types of information that advisers would be required to maintain and report, the Administration's proposal does provide a non-exhaustive list of the information to be maintained and collected. This information includes, assets under management, leverage (including off-balance sheet leverage), counterparty credit risk exposures, investment positions trading practices.

Proposal Regarding Registration of Hedge Funds. The Hedge Fund Transparency Act, which was introduced by Senators Grassley and Levin on January 29, 2009, would eliminate

Sections 3(c)(1) and 3(c)(7) of the Investment Company Act of 1940 (the "**1940 Act**") and require private investment funds to register with the SEC. Currently most private investment companies are exempt from the definition of an "investment company" pursuant to Section 3(c)(1) or 3(c)(7) of the 1940 Act and therefore are not subject to the 1940 Act. While the Hedge Fund Transparency Act would eliminate these provisions, it would incorporate them into Section 6 of the 1940 Act. As a result, a private investment fund currently relying on Section 3(c)(1) or 3(c)(7) would still be exempt from the ordinary registration and other provisions of the 1940 Act, but would be an "investment company" and have certain obligations. Any such investment company having $50 million in assets would be required to register with SEC and file an annual information form disclosing, among other things, the name and address of each investor. All funds relying on the exemptions also would be required to establish an anti-money laundering program.

SEC Proposals.

Political Contributions by Investment Advisers. On August 3, the SEC proposed a new rule under the Advisers Act that would prohibit investment advisers from (i) receiving compensation for advisory services to any government entity for a period of two years after the investment adviser or any of its "covered associates" (e.g., general partners, officers and employees who solicit government entity clients) has made a contribution to a public official or government entity that is in a position to influence the selection of investment advisers; (ii) paying third parties to solicit government entities; and (iii) coordinating contributions to candidates, elected officials or political parties where the advisor is providing or seeking to provide investment advisory services to a government entity. These prohibitions also run to government entity investments in funds, both public and private. Interestingly, this proposed rule would apply not only to registered advisers, but also to investment advisers exempt from registration pursuant to Section 203(b)(3) of the Advisers Act (the fewer than 15 client exemption). The SEC currently is seeking comments on this proposed rule.

Amendment to Custody Rule. On May 20, the SEC proposed amendments to Rule 206(4)-2 under the Advisers Act, as well as Form ADV. The amendments would require that all registered investment advisers who have or are deemed to have custody of client assets to undergo a surprise audit each year. In addition, the amendments would require investment advisers that utilize a related custodian to obtain an opinion from an independent auditor regarding such custodian's controls. The comment period on this rule has ended and we have submitted our comments (available at: http://www.sec.gov/comments/s7-09-09/s70909-677.pdf).

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The foregoing is a synopsis of the major legislative, government and regulatory proposals impacting the private investment funds industry and is not intended to be inclusive of all such proposals. Further, it is only a brief summary of the highlights of these proposals and not a thorough discussion of all details and aspects of the proposals.

If you are interested in discussing any of these proposals or its implications for your business, please contact Janet R. Murtha at (212) 984-7731.