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SECURITIES INDUSTRY PRACTICE

ALERT

SEC Extends Deadlines for Compliance by Investment Advisers and Adopts Final Registration Rules for Advisers Under Dodd-Frank

By Kimberly P. Stein

Enacted July 21, 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) introduced significant changes to the regulation of investment advisers. As part of the Dodd-Frank Act, the Securities and Exchange Commission (SEC) was tasked with adopting rules to implement the Act. The effective date of the Dodd-Frank Act is July 21, 2011.

On November 19, 2010, the SEC proposed new rules and amendments to existing rules and forms to give effect to the changes under the Dodd-Frank Act. On June 22, 2011, the SEC adopted the final rules and amendments.

The new rules implement and further clarify the changes contemplated by the Dodd-Frank Act. Of significance, the recently adopted final rules extend the July 21, 2011, effective date for investment advisers with assets under management of less than $100 million to switch from federal to state regulation and delay the registration/reporting deadline for currently unregistered private advisers. Further, the new rules implement provisions of the Dodd-Frank Act that eliminate the "private investment adviser" exemption to registration with the SEC under the Investment Advisers Act of 1940 (the 40 Act); establish new exemptions from SEC registration for small private fund advisers and venture capital fund advisers; and revise the "pay-to-play" rules.

Investment Adviser Switch for Mid-Size Advisers From Federal to State Regulation

Prior to enactment of the Act, advisers managing less than $25 million were primarily subject to state regulation and prohibited from registering with the SEC under the 40 Act. The Dodd-Frank Act raised the threshold for registration with the SEC to $100 million. Under the law, approximately 3,200 mid-sized investment adviser firms with assets under management between $25 million and $100 million will switch from federal to state regulation. While the SEC was working toward the July 21, 2011, switch date, due to needed modifications in the registration systems, the programming will not be completed by July 21, 2011. Now, advisers registered with the SEC will have to declare whether they are permitted to remain registered with the SEC in the required annual filing, which is due by March 30, 2012, and those who no longer qualify for SEC registration will be required to complete the transition to state registration by no later than June 28, 2012.

Elimination of Private Adviser Exemption and Registration/Reporting Deadline for Currently Unregistered Private Advisers

The Dodd-Frank Act eliminated the "private adviser" exemption from registration contained in Section 203(b)(3) of the 40 Act, relied on by investment advisers who had fewer than 15 clients during the preceding 12 months and who neither held themselves out to the public as an investment adviser nor served as an investment adviser to a registered investment company or business development company. The rule is designed to subject to SEC oversight and registration certain hedge funds, private equity funds and real estate funds, which are now required to register with the SEC unless another exemption is available. To facilitate the transition to SEC registration and allow these advisers to meet their obligations under the new Rules, the SEC has extended the deadline for SEC registration for currently unregistered private advisers until **March 30, 2012**.

New Exemptions From Registration for Small Private Fund Advisers and Venture Capital Fund Advisers

While the SEC has eliminated the private adviser exemption, it provides three new exemptions from registration: Small Private Fund Advisers, Venture Capital Fund Advisers and Foreign Private Advisers. However, while not required to register, there are new reporting requirements for those exempt advisers.

1. **Small Private Fund Advisers.** The SEC adopted Rule 203(m)-1 to implement an exemption for investment advisers who only advise "private funds" and who have less than $150 million in assets under management.

2. **Venture Capital Fund Advisers.** The SEC adopted Rule 203(I)-(1) to implement an exemption for firms that advise only venture capital funds. The new rule defines "venture capital fund" as a private fund that:

- Invests at least 80 percent of the fund's capital in qualifying venture capital investments (generally private operating companies);
- Does not borrow or otherwise incur leverage, other than limited short-term borrowing;
- Does not offer its investors redemption or other similar liquidity rights except in extraordinary circumstances;
- Represents itself as pursuing a venture capital strategy to its investors and prospective investors; and
- Is not registered under the Investment Company Act and has not elected to be treated as a business development company.

3. **Foreign Private Advisers.** The SEC implemented an exemption from SEC registration for foreign private advisers, defined to include advisers that do not have a place of business in the United States and have less than $25 million in aggregate assets under management from U.S. clients and private fund investors and fewer than 15 U.S. clients and private fund investors.

4. **New Reporting Requirements for Exempt Advisers.** Even though small private fund advisers and venture capital fund advisers may rely on the above exemptions from registration, these advisers will be required to file and periodically update reports with the SEC. These reports will consist of a limited number of items on Form ADV.

Changes to the Pay-to-Play Rule

The SEC has amended the investment adviser “pay-to-play” rule, which was designed to prevent an adviser from seeking to influence government officials' awards of advisory contracts through political contributions. The SEC's amendments revise the scope of the rule to apply to exempt reporting advisers and foreign private advisers. The SEC is also amending the rule to add registered municipal advisers to the categories of registered entities excepted from the rule's prohibition on advisers paying third parties to solicit government entities (provided that they are subject to the Municipal Securities Rulemaking Board's own pay-to-play rule).

At Fox Rothschild, we remain ready to assist you in assessing the impact of the SEC’s new rules on your business.
If you have any questions regarding the information in this alert, please contact:

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