Proskauer

Many Non-U.S. Advisers of Private Investment Funds Will Be Required to Register with the U.S. Securities and Exchange Commission

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Introduction

Many non-U.S. managers or advisers of private investment funds will be required to register as investment advisers with the United States Securities and Exchange Commission in order to comply with new legislation.

In particular, non-U.S. fund managers that (a) have U.S. investors in their funds or (b) manage fund vehicles established in the U.S. or (c) have a presence in the U.S. or (d) advertise in the U.S., will each need to consider the new legislation carefully.

The legislation applies to managers and advisers of private equity, private equity real estate, infrastructure, secondary and hedge funds, funds-of-funds and other private investment funds.

Background

Historically, many investment advisers to private investment funds were exempt from registration with the SEC under the U.S. Investment Advisers Act of 1940, as amended (Advisers Act), usually on the basis of the "private adviser" exemption, which generally exempted a non-U.S. adviser from registration where (a) it had less than 15 U.S. fund "clients" and (b) did not hold itself out to the public in the U.S. as an investment adviser.

Included in the Dodd-Frank Wall Street Reform and Consumer Protection Act signed into law by President Obama on 21 July 2010, is the Private Fund Investment Advisers Registration Act (Private Fund Act) which, effective from 21 July 2011, eliminates the "private adviser" exemption to the Advisers Act. Certain new, narrower, exemptions are introduced by the Private Fund Act.

Who is an "investment adviser"?

The Advisers Act defines the term “investment adviser” broadly so that it encompasses virtually any manager of or adviser to a private investment fund. It may include, depending on the circumstances, an investment adviser or investment manager of a fund exercising discretionary or nondiscretionary management or advisory functions, or a general partner of a fund constituted as a limited partnership, in each case whether U.S. or non-U.S. The precise analysis depends on the firm’s and its funds’ structure and particular circumstances.

What exemptions are available?

The Private Fund Act contains a number of new exemptions. Exemptions that are potentially relevant to non-U.S. advisers include the following:

- *Foreign Private Adviser Exemption:* The Private Fund Act exempts from registration investment advisers that have:

  (a) no place of business in the United States;

  (b) fewer than 15 clients and investors in the United States in private investment funds that are advised by such investment adviser and

  (c) less than $25 million in assets under management attributable to clients and investors in the United States.

  In addition, an investment adviser that wishes to rely on this exemption may not:

  (i) hold itself out generally to the public in the United States as an investment adviser or

  (ii) act as investment adviser to a U.S. registered investment company or a U.S. registered business development company.

  Accordingly, a non-U.S. adviser that has $25 million or more in U.S. investor money in its private investment funds (whether or not those funds are established or domiciled in the U.S.) would likely not be able to utilise this exemption.

Advisers should review the investor subscription documents for their funds to determine the level of participation by U.S. investors.

- *Private Adviser Exemption:* The Private Fund Act exempts from registration an investment adviser that acts "solely" as an adviser to private investment funds and has assets under management in the United States of less than $150 million. If an investment adviser provides advisory services to any person or entity other than a "private fund" (for example, providing advisory services directly to an institutional client pursuant to an investment management agreement), it is likely to be unable to rely on this exemption.

  The meaning of "assets under management in the United States" for the purpose of this exemption is not entirely clear and no timetable has yet been set as to when (or if) guidance will be issued by the SEC such as: Does it include both amounts (a) invested in "client" funds that are U.S. established or domiciled (such as in a Delaware limited partnership) and (b) invested by U.S. investors regardless of where the fund itself is established?

- *Venture Capital Fund Adviser Exemption:* The Private Fund Act exempts investment advisers that act as investment advisers "solely" to one or more "venture capital funds" from SEC registration. The SEC is required to adopt a definition of "venture capital funds" by 21 July 2011. It is hoped that guidance is issued on this aspect in good time to allow affected firms to register by the deadline.

- *Family Offices*: The Private Fund Act also includes an exemption for certain advisers to "family offices." The SEC is required to adopt a definition of what constitutes a "family office" that is consistent with previous exemptions for family offices.

Who has to register and by when?

Fund and fund management structures come in many forms. There may be a general partner, a manager and an adviser. In addition, a manager/adviser typically manages/advises multiple funds, which may each be structured or domiciled differently. Firms need to give detailed consideration as to which vehicle(s) will need to be registered. Absent further guidance from the SEC, it may be necessary to register more than one entity in an affiliated group.

Where registration is required, the investment adviser must register by 21 July 2011.

What are the consequences of failure to register?

Failure to comply with the registration provisions could result in civil and possibly criminal liability.

What are the SEC requirements imposed on registered investment advisers?

SEC registration brings with it a number of substantive requirements for registered advisers. For example:

- registered investment advisers will be subject to periodic announced in advance or unannounced examinations by the SEC which may last anywhere from a few days to a few months depending on the size of the firm, the results of any prior inspections and the firm's risk profile;
- registered firms must adopt an internal compliance program, including the appointment of a chief compliance officer and the creation and implementation of written compliance policies and procedures and a code of ethics;
- registered firms must make periodic filings with the SEC and must comply with requirements relating to advertising, recordkeeping and custody of client assets; and
- a registered adviser may only charge performance-based compensation (such as a carried interest) to certain types of relatively sophisticated U.S. investors (known as "qualified clients"), although this restriction does not apply to non-U.S. investors. Many U.S. investors will qualify as "qualified clients," but checks need to be made.

Where a firm that is required to register with the SEC is already regulated in another jurisdiction, such as by the Financial Services Authority in the UK, consideration will need to be given as to how to dovetail the SEC requirements with the firm's existing policies and procedures.

In the past, the SEC has granted relief from some of the requirements of registration to investment advisers that have their principal place of business outside of the United States in connection with their dealings with their non-U.S. clients.

Should you have any questions about this alert or complying with the new regulations, please contact your Proskauer relationship lawyer or any Proskauer lawyer listed in this alert.

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