Completing Form PF: A Practical Guide for Large Fund Advisers

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Completing Form PF: A Practical Guide for Large Fund Advisers

1. General Form PF requirements for large private funds
2. Large fund reporting categories
3. Large fund initial and subsequent filing deadlines
4. Specific issues for large private fund advisers when calculating thresholds and completing Form PF:
   - Related Persons / Sub-Advisers
   - Parallel Structures / Master-Feeder Funds / Fund of funds
   - Private Fund Investments
   - SEC Guidance on Specific Questions
   - CFTC Reporting Requirements
1. General Form PF Requirements

A Form PF must be filed by all advisers that:

- Are registered or required to be registered under the Investment Advisers Act of 1940

- Advise one or more “private funds” – issuers exempt from registration under the Investment Company Act of 1940 Sections 3(c)(1) or Section 3(c)(7)

- Manage at least $150 million “regulatory assets under management” attributable to private funds as of end of most recent fiscal year
1. General Form PF Requirements

Series / Classes

- Two or more series / classes of interests, each valued based on separate investment portfolios, should each be regarded as a private fund.
- Does not apply to side pocket or similar arrangements (including in vehicles such as SPVs), which should be aggregated with same series / class portfolio strategy.

“Regulatory Assets Under Management”

- Same as Form ADV
- AUM = gross of outstanding indebtedness and other accrued but unpaid liabilities
1. General Form PF Requirements

Large Private Fund Adviser Thresholds: Reporting requirements are dependent on what type of funds they advise:

- **Hedge Funds** = at least $1.5 billion in aggregate Regulatory AUM attributable to private hedge funds as of the end of any month in the prior fiscal quarter
- **Liquidity Funds** = at least $1 billion in combined Regulatory AUM attributable to liquidity funds and registered money market funds as of the end of any month in the prior fiscal quarter
- **Private Equity Funds** = at least $2 billion in combined Regulatory AUM attributable to private equity funds as of the end of any month in the prior fiscal quarter
1. General Form PF Requirements

Who completes what Form PF Sections?

Section 1 – All private fund advisers

Section 2 – Large Hedge Fund Advisers

Section 3 – Large Liquidity Fund Advisers

Section 4 – Large Private Equity Fund Advisers
1. General Form PF Requirements - Form PF Overview

Section 1:

- Section 1a - information regarding adviser’s identity and status as a large hedge fund or liquidity fund adviser
- Section 1b information about each private fund
  - Regulatory AUM and net assets aggregated by types of private funds
  - Certain information for each reporting fund (including a breakdown of level 1, 2 and 3 assets and types of investors)
  - Gross and net performance for each reporting fund
- Section 1c information about the adviser’s hedge funds
  - Description of strategy
  - Percentage of fund’s assets managed using high-frequency trading strategies
  - Trading and clearing practices
  - Significant counterparty exposures (including identity of counterparties)
  - Fund’s activities outside securities and derivatives markets
1. General Form PF Requirements - Form PF Overview

Section 2:

- Section 2a - aggregate information about each hedge fund
  - Value of assets invested in different types of securities and commodities
  - Duration
  - Weighted average tenure or 10-year bond equivalent of fixed income holdings
  - Value of turnover in certain asset classes
  - Geographical breakdown of investments
1. General Form PF Requirements - Form PF Overview

Section 2: (Continued)

- Section 2b - additional information on large hedge funds (NAV of at least $500 million as of the last day of any month in the fiscal quarter prior to the most recently completed quarter)
  - Same information as Section 2a, but on a per fund basis
  - Liquidity
  - Holdings of unencumbered cash
  - Concentration of positions
  - Fund’s base currency
  - Collateral practices with counterparties
  - Risk metrics
  - Financing information
  - Investor information
1. General Form PF Requirements - Form PF Overview

Section 3: Information about each large liquidity fund (required only by SEC; not CFTC)

- Method of computation of NAV and NAV as of month ends
- WAM / WAL – weighted average liquidity fund portfolio maturity with / without Rule 2a-7(d) exceptions (applicable to money market funds)
- Liquidity – daily, weekly, greater than 397 days
- Product exposures and portfolio concentrations
- Financing information
- Investor concentration and liquidity
1. General Form PF Requirements - Form PF Overview

Section 4: Information about each large private equity fund

- Financing and investment
- Information on controlled portfolio companies
- Geographical breakdown of investments
- Information on principal co-investment in portfolio companies
2. Large Fund Reporting Categories

Hedge Fund = any private fund having any one of three common characteristics of a hedge fund:

- A performance fee / allocation that may be paid to an investment adviser (or its related persons) that takes into account market value (instead of only realized gains)
- The ability to engage in high leverage or
- The ability to engage in short selling (except for short selling that hedges currency exposure or manages duration)

Exclusions = vehicles established for the purpose of issuing asset-backed securities
2. Large Fund Reporting Categories

“High Leverage” = borrowing by a fund

- In excess of half of NAV (including committed capital) OR
- Gross notional exposure in excess of twice the fund’s NAV (including committed capital)

**Note:** A private fund is not a hedge fund solely because organizational documents fail to prohibit borrowing or incurring derivative exposures in excess of the specified amounts or from engaging in short selling, as long as: 1) fund does not engage in these practices; and 2) reasonable investor would understand from fund offering documents that the fund will not engage in these practices – focus appears to be on what a reasonable investor would expect, based on offering documents.
2. Large Fund Reporting Categories

**Liquidity Fund** = any private fund that seeks to generate income by investing in short term obligations in order to maintain a stable NAV per unit or minimize principal volatility for investors.

**Private Equity Fund** = Any private fund that is not a hedge fund, liquidity fund, real estate fund, securitized asset fund or venture capital fund and does not provide investors with redemption rights in the ordinary course.

- Definition of “real estate fund,” “securitized asset fund” and “venture capital fund” are narrow and specific, and thus “private equity fund” is a catch-all category.
2. Large Fund Reporting Categories

- **Hedge Fund AUM** = the portion of the adviser’s Regulatory AUM that is attributable to hedge funds it advises (a threshold of $1.5 billion in hedge fund assets under management for large hedge fund adviser reporting)

- **Liquidity Fund AUM** = the portion of the adviser’s Regulatory AUM that is attributable to liquidity funds it advises (including liquidity funds that are also hedge funds) ($1 billion in combined liquidity fund and registered money market fund assets under management for large liquidity fund adviser reporting; an adviser is, however, only required to report information about unregistered liquidity funds on Form PF)

- **Private Equity Fund AUM** = the portion of the adviser’s Regulatory AUM that is attributable to private equity funds it advises ($2 billion in private equity fund assets under management for large private equity fund adviser reporting)
3. Initial Filing Deadlines

Based on Data as of June 30, 2012

- If as of last day of fiscal quarter most recently completed prior to June 15, 2012, adviser had:
  - at least $5 billion in combined assets under management attributable to liquidity funds and registered money market funds, file within 15 days of deadline (by July 15, 2012)
  - at least $5 billion in assets under management attributable to hedge funds, file within 60 days of deadline (by August 29, 2012)
  - at least $5 billion in assets under management attributable to private equity funds, as of the last day of its fiscal year to end on or after June 15, 2012 (and assuming a June 30th fiscal-year end), file within 120 days of deadline (by October 28, 2012)

Based on Data as of December 31, 2012

All other advisers, including large private fund advisers under $5 billion AUM – file within 15, 60 and 120 days of filing deadline, as applicable
3. Subsequent Filing Deadlines

- Large private equity advisers and smaller private fund advisers must file within 120 days of end of adviser’s fiscal year.

- Large hedge fund advisers must file quarterly within 60 days of end of adviser’s fiscal quarter.

- Large liquidity fund advisers must file quarterly within 15 days of end of adviser’s fiscal quarter.

- Others: within 120 days of adviser’s fiscal year end.

- Once an adviser becomes subject to quarterly reporting, it is required to update information only with respect to the type of private fund that caused it to exceed the large adviser threshold (not with respect to all of its private funds each quarter).

- An adviser must file Form PF to report that it is transitioning to only filing Form PF annually or to report that it no longer meets the requirements for filing Form PF no later than the last day on which the adviser’s next Form PF update would be timely.

General Guidance:

- If an adviser filed Form ADV Section 7.B.1 with respect to a private fund and is required to file Form PF, **that adviser must include the assets in that fund for reporting threshold purposes**

- Assets in private funds and parallel managed accounts advised by the adviser’s **non-separately-operated** “related persons” must be aggregated with the adviser’s assets

- Include all applicable assets of those “related persons” (even if they filed separate ADVs and may file separate Forms PF)

- **NOTE:** One is a separately operated related person if an adviser was **not** required to complete a Schedule D, Section 7.A on that person, *i.e.*, when:
  - No business dealings in connection with advisory services
  - No shared operations
  - No referrals to each other
  - No shared supervised persons or premises
  - No reason to believe relationship creates a conflict of interest
4. Specific Issues – Reporting Thresholds – Related Persons and Sub-Advisers

- **Note**: Where two advisers who are “related persons” manage a fund (e.g., a sub-advised fund) and one adviser reports on the fund, the other adviser does not have to report on the fund, but it still needs to include that fund’s assets in its reporting threshold calculation and, if met, it must still file Form PF.

- **Related Note**: If adviser that filed Form ADV Section 7.B.1 with respect to a private fund is NOT required to file Form PF and one or more other advisers to that fund are required to file Form PF, another adviser must include assets of that private fund for reporting threshold purposes.
4. Specific Issues – Reporting Thresholds – Related Persons and Sub-Advisers

- **Related Persons** (Form ADV, Schedule D, Section 7.A)
  - Recent SEC guidance: “filing / relying advisers” and SPVs are “related persons”
  - The “filing adviser” must
    - aggregate relying adviser’s assets for threshold purposes
  - Affiliated sub-advisers – are “related persons”
  - Advisers filing separate ADVs / Unaffiliated sub-advisers – conduct “related person” analysis
4. Specific Issues – Reporting Thresholds - Parallel Structures, Master/Feeder Funds and Funds of Funds

- For reporting threshold purposes, a reporting adviser must aggregate:
  - Dependent parallel managed accounts (SAME objective / strategy / substantially same positions as private funds) UNLESS accounts’ gross value EXCEEDS private funds’ gross value
  - Parallel funds (SAME objective / strategy / side-by-side investments in substantially SAME positions as private funds)
  - Funds that are part of SAME master-feeder arrangement (even if not permitted to aggregate for ADV Sec. 7.B.1)

- Investments in the equity of other private funds may be disregarded for threshold calculation purposes
4. Specific Issues - Individual Fund Reporting – Related persons and Sub-Advisers

General Guidance: If an adviser filed Form ADV Section 7.B.1 with respect to a private fund and is required to file Form PF, that adviser must report on that private fund.

- Related Persons (Form ADV, Schedule D, Section 7.A) - May report together on funds they advise, or separately
- Affiliated Advisers
  - Advisers filing separate ADVs – may file one Form PF
  - Filing / relying advisers - filing adviser should report on relying adviser’s funds
4. Specific Issues - Individual Fund Reporting – Related Persons and Sub-Advisers

- **Notes to General Guidance:**
  - Only report on funds that adviser and “related persons” listed in Question 1(b) advise
  - If unaffiliated sub-advisers who reported fund on Form ADV are not required to file Form PF, then Form PF reporting adviser is required to report on fund
  - Sub-advised funds will require coordination in advance, particularly where the sub-adviser is unaffiliated
    - Coordination may require amending both advisers’ Form ADV
4. Specific Issues – Individual Fund Reporting – Parallel Structures and Master/Feeder Funds

- Treatment of assets for reporting purposes:
  - Aggregate assets OR
  - Report on them separately
  - As long as reporting is done consistently throughout
  - Often, but not always, better to aggregate

- If an adviser aggregates parallel or master-feeder funds, the largest parallel / master fund is the reporting aggregate fund

- Feeder fund investments in the master fund should be disregarded but other feeder fund investments should be treated as though they were investments of the aggregate fund
4. Specific Issues – Individual Fund Reporting – Investments in Other Private Funds

- Generally: Adviser may disregard a private fund’s *equity* investments in other private funds, BUT
  - Adviser must do so consistently (e.g., do not include investments to determine whether the fund’s borrowing categorizes it as a “hedge fund” but otherwise disregard)
  - Adviser may not exclude liabilities of the private fund, even if incurred in connection with an investment in other private funds, for threshold calculation and fund reporting purposes

- Investments in non-private funds, such as registered investment companies, should be counted for all purposes
  - The adviser does not have to look through investments in those funds unless Form PF requests information regarding them or their primary purpose is to hold assets or incur leverage as part of the reporting fund’s investment activities
4. Specific Issues – Individual Fund Reporting – Funds of Funds

- Direct investments by “funds of funds” in assets that are not private funds generally must be counted toward thresholds and included in Form PF reporting
  - This includes assets that are managed by a sub-adviser, even in funds that are generally managed and marketed as “funds of funds”
4. Specific Issues – Individual Fund Reporting – Funds of Funds

- For each private fund that meets the following requirements, the reporting adviser only needs to complete Section 1b:
  - Adviser to a private fund that invests substantially all of its assets in equity of private funds [that adviser does not advise]
    - **Note**: SEC indicated that this distinction between affiliated / unaffiliated will likely go away, AND
  - Aside from private fund investments, holds only cash and cash equivalents and instruments acquired for hedging currency exposure
  - For all other purposes – disregard the fund
    - *E.g.*: do not complete Sections 1c or 2c for the fund
    - *E.g.*: do not include its assets or liabilities in aggregate info (e.g., in Section 2a)
    - *E.g.*: do not include as a qualifying hedge fund
4. Specific Issues – Large Fund Individual Reporting

Section 1b

- Update information quarterly

- Advisers should only report on individual private funds advised by related persons listed in Question 1(b)

- Advisers are not required to report information on parallel managed accounts, except in Question 11
4. Specific Issues – Large Fund Individual Reporting

Section 1b (continued)

- **Question 14:**
  - Report assets / liabilities broken down according to the categories of the fair value hierarchy (i.e., Level 1, 2 or 3) established under GAAP (FAS 157), but do not need to classify them by type
  - If GAAP is not used, an adviser can rely on the “fair value” calculation procedure in a private fund’s governing documents
  - Valuations do not need to be audited
- **Questions 15 & 16:** “beneficial owners” are same as beneficial owners under 40 Act Sections 3(c)(1) and qualified purchasers under 3(c)(7).
4. Specific Issues – Large Fund Individual Reporting

Section 1b (continued)

- **Question 17: Performance**
  - Report information for most recently completed fiscal year (or monthly or quarterly information if already being calculated)
  - Use existing methods for calculating performance reported to investors (or if not reported, used internally)
  - Performance numbers do not need to be audited
  - Report performance gross and net of management fees as well as incentive fees and allocations
4. Specific Issues – Large Fund Individual Reporting

Section 1c

- Questions 18 – 25: High-level information about each hedge fund’s potential systemic exposure
  - Update quarterly
  - Do not need to include parallel managed accounts when reporting information in Section 1c

- Question 20: Report on investment strategy by category based on NAV and (optional) capital allocation
4. Specific Issues – Large Fund Individual Reporting

Section 2b

- Update information quarterly
- Questions 29 – 50
  - “Net Asset Value” defined as gross assets reported in response to Question 8 minus outstanding indebtedness or other accrued but unpaid liabilities.
  - **Note**: Aggregation of parallel funds may result in entire structure being a qualifying hedge fund, which means information must be reported in Section 2b for each constituent hedge fund, even if some of constituent funds, individually, are not qualifying hedge funds.
4. Specific Issues – Large Fund Individual Reporting

Section 2b (continued)

- Questions 32 – 35: Advisers are allowed to rely on own methodologies in responding to these questions, provided they are consistent with info reported internally and to current and prospective investors.

- Question 33: Report information on unencumbered cash, which is defined to include “overnight repos” used for liquidity management (as long as the assets purchased are U.S. treasury securities or agency securities).
4. Specific Issues – Large Fund Individual Reporting
Section 2b (continued)

- **Question 40**: Report on Value at risk (“VaR”) during the reporting period, but only if regularly calculated for the funds during the reporting period
  - **Note**: This information will require input from adviser’s risk assessment personnel. Advisers should start identifying them and discussing form requirements with them now to ensure timely reporting of information.

- **Question 41**: Report other risk metrics considered important for monitoring risk in qualifying hedge funds
  - **Note**: The information in Form PF will be reviewed by the SEC and will be incorporated into its examinations of reporting advisers. Information should accurately reflect metrics used
  - Query whether replying “none” means that the SEC staff will consider you to be “high risk”
4. Specific Issues – Large Fund Individual Reporting

Section 2b (continued)

- **Question 42:** Report results of stress tests, if they are a regular part of formal testing
  - An adviser can omit any market factor that it did not regularly consider in formal testing, even if the adviser has considered it qualitatively
  - If there are no quantitative models, they are not required to be added to respond to the question
  - **Note:** The adviser is required to check off a box to indicate that a market factor was relevant, but not tested
  - **Query** whether this possibility virtually compels advisers to stress test all relevant factors

- **Question 43:** Report monthly breakdown of the fund’s secured and unsecured borrowing, posted collateral value and credit support, and the types of creditors
  - **Note:** To respond to this question, an adviser may have to request information from a prime broker
4. Specific Issues – Large Fund Individual Reporting

Section 2b (continued)

- **Questions 46 and 47**: Report information on financing liquidity and creditors to which the reporting fund owed amounts in respect to borrowings at 5% or greater of the reporting fund’s net asset value
  - **Note**: Financing information in Item D of Section 2b is information that FSOC must consider in determining whether to designate a non-bank financial company for FRB supervision
- **Questions 48 – 50**: Report percentage of NAV subject to side pockets, other restrictions on withdrawals and investor liquidity
  - **Note**: This information and responses to Question 32 (on portfolio liquidity) and Question 46 (on a financing liquidity), is reviewed by FSOC to determine whether a fund may have a mismatch in maturity or liquidity of its assets and liabilities, which is information FSOC must consider in determining to designate a non-bank financial company for FRB supervision
4. Specific Issues – Forms CPO-PQR and CTA-PR

CFTC adopted CFTC Rule 4.27(d) that, jointly with the SEC, establishes new reporting requirements with respect to private funds:

- Requires all CPOs and CTAs to report certain information to the CFTC on Forms CPO-PQR and CTA-PR, respectively – no exemption from reporting
- CPOs dually registered with the SEC and CFTC that file Sections 1 and 2 of Form PF, as applicable, must generally file Schedule A of Form CPO-PQR only
- Non-dually registered CPOs must file all relevant sections of Form CPO-PQR based on certain reporting thresholds
- All CTAs, regardless of SEC registration, will complete Form CTA-PR
- Both forms must be filed via NFA’s EasyFile System
4. Specific Issues – CPO-PQR Schedules, Thresholds, and Deadlines (cont’d)

- Filing requirements differ based on aggregate gross pool assets under management (“Gross AUM”) of a CPO – different from the SEC’s “regulatory assets under management” for Form PF
  - “Regulatory AUM” = assets under management attributable to private funds vs. “Pool AUM” = assets under management attributable to commodity pools on any day during the reporting period
- Large CPO = $1.5 billion in pools; Mid-Sized CPO = more than $150 million but less than $1.5 billion in pools; all others = less than $150 million
- Even if a dually registered CPO files Form PF with the SEC, it may still need to file Schedules B and/or C if it has pools that were not captured on Form PF – dual registrants may report pools on Form PF even if not a private fund
## 4. Specific Issues -- CPO-PQR Schedules, Thresholds, and Deadlines

<table>
<thead>
<tr>
<th>Assets Under Management</th>
<th>Schedule A</th>
<th>Schedule B</th>
<th>Schedule C</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dually registered – Large CPO (at least $1.5 billion AUM)</td>
<td>Quarterly – 60 days (also filing Form PF)</td>
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<tr>
<td>Dually registered – all others (less than $1.5 billion AUM)</td>
<td>Annually – 90 days (also filing Form PF)</td>
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</tr>
<tr>
<td>Large CPO (at least $1.5 billion AUM)</td>
<td>Quarterly – 60 days (not filing Form PF)</td>
<td>Quarterly – 60 days (for each pool)</td>
<td>Quarterly – 60 days (for each “Large Pool”)</td>
</tr>
<tr>
<td>Mid-Sized CPO (at least $150 million AUM)</td>
<td>Annually – 90 days (not filing Form PF)</td>
<td>Annually – 90 days (for each pool)</td>
<td></td>
</tr>
<tr>
<td>Small CPO (less than $150 million AUM)</td>
<td>Annually – 90 days (not filing Form PF)</td>
<td></td>
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</tr>
</tbody>
</table>
4. Specific Issues – CPO-PQR Initial Filing Deadlines (12/31 fiscal year)

<table>
<thead>
<tr>
<th>Commodity Pool Assets Under Management</th>
<th>Deadline</th>
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</thead>
</table>
| Large CPOs with at least $5 billion AUM in commodity pools as of last day of fiscal quarter most recently completed prior to September 15, 2012 | 60 days after September 30, 2012  
(November 29, 2012) |
| Large CPOs with between $1.5 billion and $5 billion AUM in commodity pools as of last day of fiscal quarter most recently completed prior to December 15, 2012 | 60 days after December 31, 2012  
(March 1, 2013) |
| All other CPOs | 90 days after December 31, 2012  
(March 31, 2013) |

- Rule 4.27 will become effective on July 2, 2012 and will apply to all registered CPOs regardless of whether they are still relying on Rule 4.13(a)(4) at that time
4. Specific Issues -- Form CPO-PQR, Schedule A

Schedule A seeks basic identifying information about the CPO, including:

- general information about the CPO (number of employees, name of CCO, number of pools operated)
- gross and net assets under management
- information about each of the pools operated (names of co-CPOs, foreign registrations, master/feeder status)
- Information on third party used by the pool (administrators, brokers, trading managers, custodians, auditor, marketers, etc.)
- change in assets under management and performance
- monthly rates of return
- subscription and redemption activity
4. Specific Issues -- Form CPO-PQR, Schedule B

- Only required by mid-sized (at least $150 million in pool AUM) or large (at least $1.5 billion in pool AUM) CPOs
- If completed Sections 1b and 1c of Form PF, Schedule B is only required for pools that did not meet the definition of Private Fund and the CPO did not elect to report on Form PF
- Schedule B seeks information about each pool operated by a CPO, including:
  - breakdown of the assets of the pool by investment strategies, including quantitative trading algorithms and techniques and concentrations
  - borrowings of the pool and types of creditors
  - pool counterparty and credit exposure (note the definition of “financial institution, which Form PF does not define)
  - pool trading and clearing mechanisms
  - value of the pool derivative positions
  - schedule of investments by asset types
4. Specific Issues -- Form CPO-PQR, Schedule C

- Schedule C seeks information from Large CPOs on an aggregate basis as well as on an individual pool basis for each “Large Pool”
  - “Large Pool” = any pool that has a net asset value individually, or in combination with any parallel pool structure, of at least $500mm

- A Large CPO registered as an investment adviser that operated only pools that are private funds is deemed to have satisfied Schedule C filing requirements by completing/filing Section 2 of Form PF

- Must file Schedule C for Large Pools that are not private funds or for which CPO/registered investment adviser did not elect to complete Section 2 of Form PF

- Part 1 for all pools; Part 2 for Large pools
4. Specific Issues -- CPO-PQR and Funds-of-Funds

- The treatment of investments in other funds is consistent with the instructions adopted for Form PF – a CPO may generally exclude any pool assets invested in other unaffiliated pools but must do so consistently for purposes of both thresholds and answering questions
  - However, CPO must include assets invested in other unaffiliated pools in response to Schedule A, Question 10 (changes in AUM)
  - Further, CPO may report performance of the entire pool, and need not recalculate performance to exclude investments in other pools, in response to Schedule A, Question 11 (monthly rates of return)
- CPO that operates a pool that invests substantially all of its assets in other pools for which it is not the CPO, and otherwise holds only cash and cash equivalents and instruments acquired to hedge currency exposure, must complete only Schedule A for that pool
4. Specific Issues -- Form CTA-PR

- Only Schedule A of Form CTA-PR was adopted
- Schedule A requires all CTAs to provide basic information about the CTA’s business and the pools for which it provides advice
- Form CTA-PR needs to be filed on an annual basis within 45 days after the end of the CTA’s fiscal year
- Initial filing due on February 14, 2013 for most CTAs
IV. Confidentiality

- SEC does not intend to make public any Form PF information identifiable to any particular adviser or private fund
- SEC and CFTC precluded from being compelled to reveal any information except in limited circumstances
- Information may be shared with other federal departments or agencies or SROs
- Not subject to the Freedom of Information Act
- Any information may be used in an enforcement action against adviser
- Congress is entitled to Form PF information, if requested, which introduces the risk of a politically motivated leak
Panelist Biographies
Beth Clark

AREAS OF PRACTICE
Ms. Clark is Of Counsel in K&L Gates’ Washington, D.C. office. She concentrates her practice in the investment management and securities areas where she advises participants in the financial services industry, including investment advisers, private fund managers, alternative investment vehicles and brokerage firms. In particular, Ms. Clark focuses on creating and counseling U.S. and non-U.S. private funds, including hedge funds, private equity funds and venture capital funds. She structures U.S. funds as limited liability companies, limited partnership and trusts and establishes “offshore” funds in such jurisdictions as Bermuda, the Cayman Islands and the British Virgin Islands. Ms. Clark prepares and negotiates the necessary documentation associated with private securities offerings, including disclosure and organizational documents, service provider agreements and filings and registrations, such as listing on the Irish Stock Exchange. She advises as to obligations under federal securities laws, state laws and rules, and self-regulatory organization rules.

PROFESSIONAL BACKGROUND
Prior to joining K&L Gates, Ms. Clark was an associate in the securities regulation and enforcement area of a Washington, DC law firm. Before that she practiced in New York City in the areas of investment management and mergers & acquisitions.

BAR MEMBERSHIP
District of Columbia
New York

EDUCATION
J.D., Benjamin N. Cardozo School of Law, 1999 (cum laude; Supervising Editor, Cardozo Law Review)
M.A., New York University Graduate School of Arts and Science, 1996
B.A., Cornell University, 1991
Kay Gordon

AREAS OF PRACTICE
Ms. Gordon practices in the firm’s New York office and concentrates her work in the Investment Management practice, with a particular emphasis on hedge funds, private equity funds and compliance-related matters involving registered advisers and brokers-dealers. She also advises clients on a broad range of securities and regulatory matters as well as a variety of financial instruments and transactions, including managed accounts, credit facilities, joint ventures and derivative instruments. She also represents clients in investigations by the SEC and other regulators.

Ms. Gordon was recently recognized by Legal 500 US in its 2009 Edition as a Leading Lawyer in Investment Fund Formation and Management.

PRESENTATIONS
- 3rd Annual Chief Compliance Officer Forum, New York City, March 12, 2008.
Kay Gordon


PUBLICATIONS

- “SEC Proposes Amendments to the Qualified Client Standard,” VC Experts, June 6, 2011.
- “Firms Look to Peers on IT Security,” Compliance Reporter, September 8, 2008 — Ms. Gordon’s quote was selected as a “Quote of the Week.”
- Co-Author, “Blending FSA and SEC Rules for Dual-Regulated Non-US
Kay Gordon


PROFESSIONAL/CIVIC ACTIVITIES
- CFA, chartered financial analyst, 2003
- Association for Investment Management and Research
- Stamford Society of Security Analysts
- American Bar Association, Committee on Investment Management

BAR MEMBERSHIP
New York

EDUCATION
J.D., University of Pennsylvania School of Law, 1997
B.A., Allegheny College, 1994 (magna cum laude, Phi Beta Kappa)

ACHIEVEMENTS
- Selected as a “Leading Lawyer” in Investment Fund Formation and Management, 2009 Legal 500 US

LANGUAGES
Russian
Mark D. Perlow

AREAS OF PRACTICE
Mr. Perlow’s practice focuses on investment management and securities law. He regularly represents mutual funds, hedge fund managers, investment advisers, fund boards of directors, and broker-dealers on a variety of regulatory and transactional matters. He has represented clients on a broad range of traditional and novel matters, including:

- Representing funds, investment advisers, and broker-dealers before the SEC and FINRA in connection with registration, exemptive applications, no-action and interpretive requests, enforcement actions, examinations, and transactional and disclosure filings
- Forming and reorganizing mutual funds as well as preparing and negotiating the full range of fund documents and agreements
- Structuring and forming hedge funds
- Counseling and negotiating agreements for funds, investment advisers and broker-dealers on issues arising from distribution (including retirement plan issues) and on counseling on regulatory issues in marketing and advertising
- Representing and advising fund independent directors
- Serving in interim role as chief legal officer for major investment manager and mutual fund sponsor
- Advising and assisting clients on adviser and fund mergers, acquisitions and adoptions
- Conducting “mock” SEC examinations and compliance reviews
- Advising funds on legal and regulatory aspects of derivatives, short selling, and market structure
- Counseling clients on “investment company,” “investment adviser” and “broker-dealer” status issues
- Representing and advising the Investment Company Institute on regulatory policy recommendations and preparing related SEC submissions
- Preparing comments on SEC rule-making
- Advising fund sponsors and investors on regulatory and market issues posed by exchange-traded funds
- Serving as expert witness on industry practices
- Counseling clients on compliance with the Dodd-Frank and Sarbanes-Oxley Acts
- Advising clients on fiduciary duties and corporate governance, including proxy voting responsibilities
- Advising and assisting fund sponsors on new investment vehicles, including funds of hedge funds, alternative strategy mutual funds, 130/30 funds, employees’ securities companies, manager-of-managers funds, stable value funds and basket depositary receipts

PROFESSIONAL BACKGROUND
Mr. Perlow served as senior counsel in the Office of the General Counsel of the Securities and Exchange Commission from 1998 to 1999, focusing on investment
Mark D. Perlow

management, fund and corporate governance, and enforcement. He also served in the SEC’s Division of Enforcement from 1994 to 1997. While on the SEC staff, Mr. Perlow worked on regulatory initiatives on fund governance, the scope of the securities laws online, codes of ethics, personal trading of investment personnel, and foreign custody of fund assets, and he advised the SEC on enforcement actions involving funds and investment advisers.

He also served as senior attorney on a number of enforcement actions and investigations, including the W.R. Grace 21(a) Report on independent directors’ duties, and cases involving accounting fraud, market manipulation, insider trading, and broker-dealer sales abuses. Prior to government service, Mr. Perlow was associated with a California law firm and represented technology companies on corporate, securities, and intellectual property matters.

PROFESSIONAL/CIVIC ACTIVITIES

- American Bar Association (Member of Committee on Federal Regulation of Securities and Subcommittee on Investment Companies and Investment Advisers, Task Force on Investment Company Use of Derivatives and Leverage)
- Federal Bar Association
- Hedge Funds Care, West Coast Committee
- West Coast ’40 Acts Group
- National Investment Company Service Association (West Coast Steering Committee)
- Adjunct Faculty, U.C. Berkeley School of Law, “Capital Markets and Financial Institutions: Crisis and Regulatory Response,” Fall 2009 and 2010

BAR MEMBERSHIP

California
District of Columbia

EDUCATION

J.D., Yale Law School, 1991 (Executive Editor, Yale Journal on Regulation, Olin Fellow in Law, Economics and Public Policy)
M.A., Oxford University, 1988 (Newton-Tatum Scholar)
A.B., University of California, Berkeley, 1986 (summa cum laude)

PUBLICATIONS

Articles

Mark D. Perlow


Client Alerts and Updates
- “Sweeping Reforms Moving Forward for Credit Rating Agency Practices,”
Mark D. Perlow

Investment Management Alert, October 13, 2009.
• Global Financial Markets – Legal, Policy and Regulatory Analysis, Volume 1, Issue 1, October 6, 2008.
• “SEC and FSA Take Actions Against Short Selling,” Investment Management and Hedge Funds Alert, September 19, 2008.
Mark D. Perlow

PRESENTATIONS

Mr. Perlow is a frequent speaker and panelist on subjects related to the investment management industry. His recent presentation topics include:

- the Dodd-Frank Act
- regulatory initiatives regarding hedge funds, private equity funds and their managers
- regulation of derivatives and funds’ use of derivatives
- regulation of portfolio management and investment risk
Shoshana L. Thoma-Isgur

AREAS OF PRACTICE
Shoshana Thoma-Isgur is of counsel in the firm’s Fort Worth office. Her practice focuses on investment management and securities compliance matters, including investment fund formation, structure, management, compliance with federal and state securities regulations, and regulatory examinations. Shoshana also works on federal and state securities enforcement matters.

PROFESSIONAL BACKGROUND
While at K&L Gates, Shoshana worked on secondment as a global adviser to a private fund complex to help register the adviser and build its compliance program.

Before joining K&L Gates, Shoshana was an Enforcement attorney in the SEC’s Fort Worth Regional Office (FWRO). While at the FWRO, Shoshana investigated numerous matters, which resulted in over 20 enforcement and criminal actions. She also participated in multiple SEC cases and administrative proceedings. Shoshana was a member of the SEC’s Asset Management Unit, where she specialized in investment adviser/ investment company disclosure and drafted Enforcement Division reference materials on the Investment Company Act of 1940 and the Investment Advisors Act of 1940. She also oversaw and made numerous public and CLE presentations on the FWRO’s investor fraud education program. Before joining the SEC, Shoshana worked at a Texas law firm on corporate and securities issues.

PUBLICATIONS
- “SEC Enforcement Action Shows Regulatory Focus on Private Equity Managers,” VC Experts, October 27, 2011
- “SEC Enforcement Actions Shows Regulatory Focus on Private Equity Managers,” Investment Management Alert, October 3, 2011

PROFESSIONAL/CIVIC ACTIVITIES
- Member, Girl Scouts of Texas Oklahoma Plains Community Partners Advisory Council
- Former President and Board Member, Jewish Education Agency
- Fort Worth YMCA Volunteer
- Former Board Member and Chairperson for annual fundraiser, Jewish Federation of Fort Worth & Tarrant County

BAR MEMBERSHIPS
Texas

COURT ADMISSIONS
- The Supreme Court of Texas
- Northern District of Texas
Shoshana L. Thoma-Isgur

EDUCATION
J.D., St Mary’s University School of Law, 1998 (cum laude; Member, Harlan Honor Society)
B.A., The University of California at Santa Barbara, 1990

ACHIEVEMENTS
Securities and Exchange Commission
- SEC Chairman’s Award for Excellence
- SEC Enforcement Director’s Award

Jewish Federation of Fort Worth & Tarrant County
- Barnett Young Leadership Award for Outstanding Service and Leadership
Additional Materials
SEC, CFTC Adopt Form PF for Systemic Risk Data Reporting by Private Fund Advisers

By Arthur C. Delibert and Mark D. Perlow

The SEC on October 31, 2011 adopted Form PF, which will be used to collect information from private fund advisers, primarily to assist the Financial Stability Oversight Council (“FSOC”) in determining whether any such funds present systemic risks to the U.S. financial system. The SEC also adopted Rule 204(b)-1 under the Investment Advisers Act of 1940, requiring private fund advisers to file the form. At the same time, the CFTC adopted Sections 1 and 2 of the form and Rule 4.27 under the Commodity Exchange Act, requiring commodity pool operators and commodity trading advisors that are also registered with the SEC as private fund advisers to report on Form PF. The Dodd-Frank Wall Street Reform and Consumer Protection Act, enacted in July 2010, directs the two agencies to adopt such reporting requirements.

Although the Form remains lengthy and detailed, the agencies made a number of adjustments intended to accommodate the manner in which they believe private fund advisers actually calculate various parameters and keep their internal records. They also extended the initial filing deadlines well into 2012. The Form retains the graduated reporting scheme proposed by the agencies in January and adds a new tier: small entities are exempt from reporting altogether, and beyond that, all advisers to private funds must file at least the basic information called for by Section 1 of the Form. Larger managers of hedge funds, liquidity funds and private equity funds must file the additional information required by Sections 2a, 3 and 4 of the Form, respectively, and managers of the largest hedge funds must file further detail under Section 2b.

While this alert summarizes the elements of the Form and requirements for compliance with the implementing rules, it cannot do justice to their complexity. The alert is divided into sections that provide an overview of different aspects of the rule or parts of the Form, starting with a description of significant changes from the proposed rule and Form and the threshold requirements determining which advisers must file the Form. The alert summarizes Part 1, which all filing advisers must complete; Part 2, which hedge fund advisers and CFTC registrants must complete; Part 3, which liquidity fund advisers must complete; and Part 4, which private equity fund advisers must complete. Next, the alert analyzes the policy purposes for which the information on the Form will be used and the confidentiality protections (such as they are) provided by the regulators. The alert concludes with a summary of the rule’s effective dates, the phased commencement of filing requirements, and the required frequency of filing.

2 See our previous Client Alert titled, “SEC and CFTC Propose New Forms to Gather Data on Systemic Risk Potentially Presented by Private Funds” here.
What Changed From the Proposal

Perhaps most importantly, the General Instructions now allow advisers to use their existing methods to calculate most of the data they are required to report, “provided the information is consistent with the information [the adviser reports] internally and to current and prospective investors.” (General Instruction 15.) Internal methods used for reporting on Form PF must be consistently applied and consistent with agency instructions and guidance. This change should save many advisers from having to make costly revisions to their systems. It was apparently adopted in recognition that FSOC needs the data to identify broad characteristics and general trends; precise comparability is not necessary, provided that all advisers are calculating the data using reasonable methods applied in good faith. In addition, the certification for the Form will not require (as was proposed) that the signing individual affirm the statements in the Form under penalty of perjury, in recognition that completing the Form requires estimates and the exercise of judgment.

Indeed, the release is unusually responsive to industry comments, particularly in seeking to explain the justification for many of the decisions that went into creating the final rule. Thus, we may actually be seeing in this release the SEC’s response to the recent decision of the U.S. Court of Appeals for the D.C. Circuit in Chamber of Commerce of the U.S. vs. SEC, where the court was sharply critical of the caliber of the agency’s cost-benefit analysis. Interestingly, the release at one point explicitly shifts the responsibility to FSOC for much of the content of the form:

The policy judgments implicit in the information required to be reported on Form PF reflect FSOC’s role as the primary user of the reported information for the purpose of monitoring systemic risk. The SEC would not necessarily have required the same scope of reporting if the information reported on Form PF were intended solely for the SEC’s use (release at 8).

Who Must File

An adviser must file at least Part 1 of Form PF if it (1) is registered or required to register as an investment adviser with the SEC; (2) advises one or more “private funds”; and (3) had at least $150 million in regulatory assets under management attributable to private funds as of the end of the adviser’s most recently completed fiscal year. A “private fund” is one that would have to register with the SEC under the Investment Company Act of 1940 but for the exclusions from the definition of “investment company” contained in Sections 3(c)(1) and 3(c)(7) of that Act. The method to calculate “regulatory assets under management” is the same one specified in Form ADV.

In making the calculation of assets under management attributable to private funds, advisers must aggregate together assets of managed accounts or pools of assets (including registered funds) advised by the firm that “pursue substantially the same investment objective and strategy and invest in substantially the same positions” as private funds advised by the firm (“parallel managed accounts”), unless the value of those accounts exceeds the value of the private funds with which they are managed. Thus, a firm would be deemed to meet the $150 million reporting threshold if it had $76 million in private fund assets and $75 million in parallel managed accounts, but would not meet the threshold if it had $75 million in private fund assets and $76 million in parallel managed accounts.

Advisers also must aggregate with their own funds assets of private funds advised by any of the adviser’s “related persons” other than related persons that are separately operated. An adviser’s

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3 Note that the calculations of reporting thresholds are not items for which Form PF permits advisers to use their own methods of calculation.
“related persons” include all of its officers, partners, directors and employees (other than those performing only clerical, administrative or support functions) and any person directly or indirectly controlling, controlled by or under common control with the adviser. The exclusion for separately operated persons is a change from the rule as it was proposed, in response to industry comments noting that aggregation across related persons may not be practical or even possible for large institutions that operate under separate business units with independent decision-making. The standard for separateness is that set forth in Item 7.A of Form ADV, which focuses on business dealings, shared operations and personnel, referrals and conflicts of interest. The SEC believes that reference to this standard in Form PF should create a minimal additional burden, since advisers will already have had to consider its application to their own operations.

For purposes of both these reporting thresholds and responding to items in the Form, an adviser may exclude any assets invested in the equity of other private funds. And, if a fund invests substantially all of its assets in other private funds and certain cash instruments, its adviser may disregard the fund for all reporting except section 1b (see below). These provisions are intended to avoid duplicative reporting by funds of funds and related structures. An adviser and its related persons may, but are not required to, report their private fund assets on a single Form PF. An adviser also may provide information regarding master-feeder arrangements and parallel funds structures in the aggregate or separately, provided that it is done consistently.

Certain foreign advisers are exempt from reporting certain funds in order to avoid duplication with foreign regulatory reporting requirements. Specifically, if the adviser’s principal office and place of business are outside the U.S., the adviser can disregard any private fund that, during the adviser’s fiscal year, was not a U.S. person (as defined in rule 203(m)-1 under the Investment Advisers Act, which largely tracks the definition in Regulation S), was not offered in the U.S., and was not beneficially owned by any U.S. person.

Basic Reporting Requirements for All Filers – Part 1 of Form PF

Section 1a of Form PF requires basic census-type information about each reporting adviser, including identifying information and basic aggregate data about size and assets attributable to certain types of private funds. Section 1b requires basic information about each private fund managed by the adviser; the adviser must complete a separate Section 1b for each private fund it manages (other than master-feeder structures, where the adviser is permitted to report on the structure in the aggregate). Section 1b calls for information on gross and net assets, liquidity, aggregate notional value of the fund’s derivative positions, borrowings and creditors, ownership character and concentration, and performance. In response to industry comments, the SEC made two changes to the performance reporting requirements: first, while advisers are required to report performance for the fund’s most recently completed fiscal year, they are not required to report monthly and quarterly performance unless that information is already being calculated for the fund. Second, in this area advisers are permitted to use their existing methods for calculating performance.

The SEC added two questions to Section 1b that had originally been proposed as part of Form ADV – one requiring advisers to report assets and liabilities broken down according to the categories of the fair value hierarchy (i.e., Level 1, 2 or 3) established under U.S. generally accepted accounting principles (“GAAP”) and the other requiring information on the approximate percentage of each fund owned by certain types of investors. While advisers commenting on the proposed Form ADV had raised concerns about the burden of providing such breakdowns, the agencies stated their belief that most private fund organizations are already using GAAP or similar accounting. They also noted that
the questions are aimed at understanding the potential for private funds to be caught in a liquidity crunch, a subject of particular interest to the FSOC.

Section 1c of the Form asks for information about each hedge fund the adviser manages. This section seeks high-level information about a fund’s potential systemic exposure. Thus, it asks about the fund’s investment strategy by category (e.g., equity, macro, relative value, event-driven), the degree of use of high-frequency trading, the five counterparties to which the fund has the highest credit exposure, and the use (or non-use) of central and bilateral trading and clearing mechanisms. The item directed at high-frequency trading alone indicates that it is likely that the Commissions will use information from the Form to target fund advisers for examination and further inquiry based on larger policy and political concerns.

Large Hedge Funds – Part 2 of Form PF

An adviser having at least $1.5 billion in regulatory assets under management attributable to hedge funds as of the end of any month in the prior fiscal quarter must file Part 2 of Form PF. The rules on aggregating parallel managed accounts, discussed above, apply to this threshold calculation as well. These reports must be filed quarterly.

For purposes of Form PF, a “hedge fund” is a private fund having any one of the following characteristics: (1) an adviser to the fund may be paid a performance fee or allocation that takes into account unrealized gains; 4 (2) the fund may borrow an amount in excess of one-half its net asset value or may have gross notional exposure more than twice its net asset value (including, in each case, any committed capital); or (3) the fund may sell securities or other assets short or enter into similar transactions. Furthermore, under CFTC filing requirements, “solely for purposes of Form PF, a commodity pool that is reported or required to be reported on Form PF is treated as a hedge fund.” In response to industry comments, the SEC expressly excluded from the definition of “hedge fund” vehicles established for the purpose of issuing asset-backed securities, as it was not the agency’s intent to capture such vehicles in the Form PF reporting regime. The SEC also excluded from the third characteristic above short selling that hedges currency exposure or manages the duration of interest rate exposure. It did, however, also clarify that the definition includes funds that take short positions through the use of derivative instruments; that is, the important factor is the economic position of the fund, not its method of achieving it.

The release also reiterated that a private fund is considered a hedge fund not only if it pays a performance fee or uses leverage or short selling as described above, but if it may do so. The release notes that even funds that often engage in such practices may not do so every quarter; if such funds ceased reporting during these periods, it could result in incomplete data sets for hedge funds, “a class of funds that may be systemically significant.” At the same time, however, the SEC stated that --

… a private fund would not be a “hedge fund” for purposes of Form PF solely because its organizational documents fail to prohibit the fund from borrowing or incurring derivative exposures in excess of the specified amounts or from engaging in short selling so long as the fund in fact does not engage in these practices … and a reasonable investor would understand, based on the fund’s offering documents, that the fund will not engage in these practices.

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4 The SEC indicated that this prong of the definition was not intended to capture private equity funds, and it excluded funds that calculate performance fees taking into account unrealized gains solely for the purpose of reducing such fees to reflect net unrealized losses.
However, there is a vast range of possibilities between the broad definition and the narrow and vague exclusion described above. But the SEC’s focus appears to be on what a reasonable investor would understand the fund’s practices to be, based on the offering documents.

As adopted, the test to determine which firms have to complete Part 2 contains two changes from the original proposal. First, the reporting threshold has been increased from $1 billion to $1.5 billion in regulatory assets. Second, the proposal would have imposed the reporting requirements of Part 2 on any adviser that met the threshold at any time during the prior quarter (rather than at the end of any month in that quarter). The SEC accepted industry arguments that advisers of hedge funds simply do not value fund assets every day. The agency also agreed that a monthly calculation was sufficient to provide the FSOC with the data it needs, and at the same time to minimize the danger of “window dressing” – i.e., advisers temporarily restructuring their portfolios just before the measurement date to avoid having to report.

The information required in Section 2a is data aggregated across all the hedge funds managed by the adviser, including the aggregate value of assets invested (on a long and short basis) in different types of securities, derivatives and commodities, the turnover rate in certain asset classes, and a geographical breakdown. The Commissions did revise somewhat the data required in response to Section 2a, based on the comments they received. For example, a question that, as proposed, had asked for information on the duration of fixed income securities has been modified to allow reporting of duration, weighted average tenor or 10-year bond equivalents, because commenters noted that different advisers use different metrics to measure interest rate sensitivity.

Section 2b applies only to hedge funds with at least $500 million in net assets as of the end of any month in the prior fiscal quarter, which the Form terms “qualifying hedge funds.” In calculating a fund’s net assets, an adviser must aggregate any parallel funds, funds that are part of the same master-feeder arrangement and, as discussed above, parallel managed accounts and parallel funds of related persons. Note that if the aggregation of parallel funds results in the entire structure being a qualifying hedge fund, data must be reported in Section 2b for each constituent hedge fund, even if some of the constituent funds, considered individually, are not large enough to be qualifying hedge funds.

This section requires separate information with respect to each qualifying hedge fund. In addition to a fund-by-fund break-out of certain data presented on an aggregate basis in Section 2a, Section 2b requires an adviser to report on portfolio liquidity, holdings of unencumbered cash and concentration of positions. According to the release, these questions have been modified from the proposal “to allow advisers to rely more on their own methodologies in responding.” The section also requests a range of additional information about each reporting fund’s top five counterparties, including the collateral posted by the fund to the counterparty and vice versa and the amount that can be rehypothecated.

Section 2b also requires advisers to report a variety of possible risk metrics for their qualifying hedge funds, but only if the adviser regularly calculated those metrics for the funds during the reporting period. One such risk metric is value at risk (“VaR”), which the SEC staff believes is widely used for all but the most illiquid strategies. Responding to concerns that a negative response to this question would give rise to an inference that the adviser is not prudently managing the fund’s risk, the agencies

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5 This change is not quite what it appears to be. The release explains that in setting the proposed standard, agency staff had considered industry data that was based on net assets under management, while the calculation of regulatory assets under management captures gross assets. Thus, the regulators expect that a threshold of $1.5 billion in gross assets attributable to hedge funds will capture much the same group of advisers as the prior threshold would have, roughly 250 large hedge fund managers.
have added a new question asking advisers to report metrics other than, or in addition to, VaR that they may consider important in managing the fund’s risk.

As it was proposed, Section 2b also asked for the results of certain stress tests, if they are a regular part of the adviser’s formal testing. This question has been modified to permit an adviser to omit any market factor that it did not regularly consider in formal testing, even if the adviser has considered it qualitatively. The release reiterates that those advisers without existing quantitative models will not be required to add them to respond to the question. The Commissions have gone a long way in addressing concerns about the proposed Form that it would have required advisers to perform stress testing; however, the length and detail of this section of the Form may be taken to suggest that advisers that do not conduct formal testing are not managing their risks appropriately, and it would not be surprising if the Commissions view advisers that do not provide responses to the questions in this section as higher-risk firms for further examination.

In addition, Section 2b asks questions aimed at identifying mismatches between a qualifying hedge fund’s assets and its liabilities, including a monthly breakdown of the fund’s secured and unsecured borrowing, the value of posted collateral and credit support, and the types of creditors. The release states that this information is intended to assist FSOC in identifying funds that may be subject to failure from investor redemptions during times of market stress. Finally, the Form requires the fund adviser to report a range of information about the composition of the fund’s investors and their liquidity rights, including information about side-pocket, gating and lock-up arrangements; this information is designed to allow monitoring of the fund’s susceptibility to failure through redemptions under conditions of stress.

**Liquidity Funds – Section 3**

Advisers to “liquidity funds” must provide the detailed information called for in Section 3 of Form PF if the fund had at least $1 billion in combined regulatory assets under management attributable to liquidity funds and registered money market funds as of the end of any month in the prior fiscal quarter. A “liquidity fund” is a private fund that seeks to generate income by investing in a portfolio of short-term obligations in order to maintain a stable net asset value per share or minimize principal volatility for investors. The timing of the test – as of the end of any month in the prior fiscal quarter – represents a change from the proposal, which would have required filing if the adviser’s liquidity fund assets under management reached the $1 billion threshold on any day during the quarter. An adviser required to report on Section 3 must report quarterly and provide the requested information for each liquidity fund that the adviser manages.

Section 3 was adopted with few changes from the proposal. The adviser must report certain identifying information, as well as the net asset value of the fund, the weighted average maturity and life of the fund, its 7-day gross yield and information about the liquidity fund’s assets. The adviser also is required to report the fund’s exposures to different types of assets (e.g., sovereign debt and instruments issued by financial institutions both in and out of the U.S.) by ranges of maturities, as well as the amount and type of the fund’s borrowings. Finally, Section 3 requires that the adviser report on the composition and concentration of the fund’s investors and the liquidity of their fund interests. This information is designed to assist the regulators in assessing these funds’ “susceptibility to runs” and their potential for “contagion” to money market funds or other liquidity funds.

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6 The SEC notes that liquidity funds can resemble registered money market funds and states that certain of their features may make them susceptible to runs and thus create the potential for systemic risk.
Private Equity Funds – Section 4

An adviser managing one or more “private equity funds” must provide the detailed information called for in Section 4 of Form PF if the adviser had at least $2 billion in combined regulatory assets under management attributable to “private equity funds” as of the last day of the adviser’s most recently completed fiscal year. A “private equity fund” is a private fund that is not a hedge fund, liquidity fund, real estate fund, securitized asset fund or venture capital fund (as those fund types are defined in Form PF) and that does not provide investors with redemption rights in “the ordinary course” (which the SEC does not define). The principal change from the proposed rule relates to the frequency of reporting: the SEC agreed with commenters that the parameters of private equity funds usually change much more slowly than those of hedge funds and liquidity funds. Accordingly, advisers to large private equity funds are required to complete Section 4 only on an annual basis.

Beyond that, however, the section is little changed. The SEC, in consultation with the FSOC member agencies, continues to be concerned about the potential risk that private equity funds pose to lending institutions when bridge loans cannot be syndicated or refinanced and the potential leverage that a private equity fund may impose on its portfolio companies, especially financial industry companies. The release cites a study that found private equity funds often enjoy favorable terms in their bank financing because of their sponsors’ close relationships with the lending banks.

Thus, in addition to questions asking for identifying information and a geographical and sector breakdown of investments, the Section 4 questions primarily focus in detail on the leverage, capital structure and borrowings of “controlled portfolio companies,” i.e., those portfolio companies as to which the private equity fund has the power, directly or indirectly, to direct the management or policies of a person, whether through ownership of securities, by contract, or otherwise. While commenters raised concerns that the threshold of “control” was too low and did not necessarily equate to an ability to obtain the necessary information, the SEC rejected these concerns, stating that the questions have been redesigned so that much of the required information is available from the financial statements of the portfolio companies or relates to the fund’s own investments in the companies.

Uses of the Data Collected on Form PF

As noted, the release states that the primary purpose for gathering the data is to assist FSOC in understanding and monitoring systemic risk in the private fund industry. FSOC scrutiny could result in recommendations to the primary regulators of private funds that they be subject to more stringent regulation. FSOC also may work with the Office of Financial Research to obtain more detailed information from particular companies. And, FSOC may recommend that particular private funds, on the basis of the risk they are believed to pose to the stability of the U.S. financial system, be subject to prudential regulation by the Federal Reserve Board.

The release also notes that the SEC and the CFTC “may” (i.e., will) use the information they collect on Form PF “in their regulatory programs, including examinations, investigations and investor protection efforts relating to private fund advisers.” Since the two Commissions, and the SEC in particular, will be viewed by Congress and the public as the frontline regulators of private fund managers on all issues, including systemic risk, this use of Form PF information has the potential to change the character of Commission examinations and will certainly place more tools at the disposal of examiners in determining the riskiness of registered advisers and areas of focus for examinations.
Confidentiality of the Data

Data submitted on Form PF is deemed confidential under both the Investment Advisers Act and the Commodity Exchange Act. Furthermore, the instructions to the Form note that an adviser can preserve the anonymity of a fund by designating it with a numerical or alphabetical code both in the adviser’s records and on the Form.

Although the data may be shared with other departments or agencies and securities industry self-regulatory organizations, the release states that these other entities also are exempt from being compelled under the federal Freedom of Information Act to disclose the information. The release states that the SEC and the CFTC, prior to sharing Form PF data with other entities, intend to require such entities to represent that they have in place controls designed to ensure the information is handled in a manner consistent with the protections established by the Dodd-Frank Act (although it is difficult to imagine that the SEC or CFTC would actually go behind such a representation to assure itself that an agency has adequate policies and procedures to carry out those controls).

The release does note, however, that the agencies may use Form PF information in an enforcement action, in which case, although the release does not say it in so many words, the information would potentially be subject to public disclosure. In addition, the Dodd-Frank Act requires the SEC to share the information gathered on the Form with Congress, under agreement of confidentiality. Recent disclosures of confidential energy contract trading information provided to Congress indicate that advisers submitting the Form can take only a certain amount of comfort in such Congressional agreements.

Effective Date, Commencement and Frequency of Filing Requirements

The SEC has staggered the dates of the initial filings depending on the size of the funds that an adviser manages. The effective date for both CFTC Rule 4.27 and SEC Rule 204(b)-1 is March 31, 2012. The dates for initial filing of Form PF are phased. Specifically, the compliance date is June 15, 2012 for any adviser having –

- assets under management of at least $5 billion attributable to hedge funds as of the last day of the adviser’s fiscal quarter ending most recently before June 15, 2012 (such an adviser must make its first filing within 60 calendar days after June 30, 2012);
- assets under management of at least $5 billion attributable to liquidity funds and registered money market funds as of the last day of the adviser’s fiscal quarter ending most recently before June 15, 2012 (such an adviser must make its first filing within 15 calendar days after June 30, 2012); or
- assets under management of at least $5 billion attributable to private equity funds as of the last day of the adviser’s first fiscal year to end on or after June 15, 2012 (such an adviser must make its first filing within 120 calendar days after June 30, 2012).

For all other advisers, the compliance date is December 15, 2012. Such advisers, if they have calendar-year fiscal periods, would file based on the information as of December 31, 2012.

Large hedge fund advisers must file their information as to all hedge funds they manage within 60 days after the end of each fiscal quarter. Large liquidity fund advisers must file as to all liquidity funds they advise within 15 days after the end of each quarter. An adviser with both large hedge funds and large liquidity funds is subject to the 60-day deadline for the former and the 15-day deadline
for the latter. Either type of adviser can file its annual update of the remainder of Form PF at that
time, or it can wait until 120 days after the fiscal year-end and update the remainder at that time. If an
adviser chooses the latter timing, it is not required at the 120-day mark to update the quarter-end
information filed at the 15- or 60-day mark. Those that are not large fund advisers, and advisers that
manage only private equity funds, are required to update within 120 days of the end of each fiscal
year.

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