



## SEC ADOPTS RULES IMPLEMENTING DODD-FRANK'S EXEMPTIONS FROM REGISTRATION UNDER THE INVESTMENT ADVISERS ACT

On June 22, 2011, the Securities and Exchange Commission adopted rules under the Investment Advisers Act of 1940 ("Advisers Act") implementing provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank") with respect to exemptions for certain persons from registration as an investment adviser under the Advisers Act.

Prior to Dodd-Frank, a common exemption from registration that many persons relied upon, referred to as the "private adviser" exemption, exempted from registration persons (i) with 14 or fewer clients during the preceding 12 months, (ii) who did not hold themselves out to the public as investment advisers, and (iii) did not act as an investment adviser to a investment company registered under the Investment Company Act of 1940 ("Investment Company Act") or a business development company. The private adviser exemption was repealed by Dodd-Frank. By March 30, 2012, persons relying on the private adviser exemption must either register under the Advisers Act or otherwise fit within another exemption.

Dodd-Frank, however, created several new exemptions from registration: the private funds adviser exemption, the foreign private adviser exemption, and the venture capital funds adviser exemption, each of which are summarized below.

### ***Private Funds Adviser***

Dodd-Frank required the SEC to provide an exemption from the registration requirements to any person acting solely as an adviser to private funds who has assets under management in the United States of less than \$150 million.

There are two important tests to determine whether a person meets this exemption. First, the person may provide investment advice *solely* to private funds. A private fund is a fund that is exempt from registration under Investment Company Act Section 3(c)(1) (funds with less than 100 beneficial owners) or Section 3(c)(7) (funds whose beneficial owners are solely qualified purchasers). Other exempt funds, such as a real estate fund relying on the exemption contained in Section 3(c)(5)(C) of the Investment Company Act, may still be a private fund.

The second test is whether the person has assets under management in the United States of less than \$150 million. Generally, this is calculated by aggregating the gross value (before deducting any liabilities) of all assets of private funds the adviser manages, including proprietary assets, assets managed without compensation, and uncalled capital commitments.

Advisers relying on this exemption must annually calculate the amount of the private fund assets under management and report these amounts in annual amendments on Form ADV. Advisers reporting \$150 million or more of private fund assets under management no longer qualify for the private fund adviser exemption. Section 203A(a)(2) of the Advisers Act defines "assets under management" as the "securities portfolios" with respect to which an adviser provides "continuous and regular supervisory or management services."

The tests are different for foreign advisers. All private fund assets of an adviser with a principal office and place of business in the United States are considered to be assets under management in the United States. However, an adviser with a principal office and place of business outside of the United States need

only count private fund assets it manages at a place of business in the United States toward the \$150 million asset limit.

### ***Foreign Private Adviser***

Dodd-Frank, as clarified by the SEC's new rules, exempts from registration under the Advisers Act any foreign private adviser. A "foreign private adviser" is any investment adviser that:

- has no place of business in the United States;
- has, in total, fewer than 15 clients in the United States, including investors in the United States in private funds advised by the investment adviser;
- has less than \$25 million aggregate assets under management attributable to clients in the United States; and
- does not hold itself out generally to the public in the United States as an investment adviser.

### ***Venture Capital Funds Adviser***

Dodd-Frank amended the Advisers Act to provide that a person who acts as an investment adviser solely to venture capital funds is exempt from registration under the Advisers Act. The SEC's new rule defines a "venture capital fund" as a "private fund" that:

- holds no more than 20% of the fund's capital commitments in equity securities directly acquired from qualifying portfolio companies (as defined below);
- 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.

The SEC defines a "qualifying portfolio company" as any company that:

- is not a reporting or foreign traded company and does not have a control relationship with a reporting or foreign traded company;
- does not incur leverage in connection with the investment by the private fund and distribute the proceeds of any such borrowing to the private fund in exchange for the private fund investment; and
- is not itself a fund.

### ***Reporting***

Although exempt from registration under the Advisers Act, advisers relying on the private funds adviser exemption or venture capital funds adviser exemption must submit to the SEC certain reports. Such reports will require the following information: Part 1A of Form ADV: Items 1 (Identifying Information), 2.B. (SEC Reporting by Exempt Reporting Advisers), 3 (Form of Organization), 6 (Other Business Activities), 7 (Financial Industry Affiliations and Private Fund Reporting), 10 (Control Persons), 11 (Disclosure Information), and Schedules A, B, C, and D.

These reports must be filed with the SEC electronically on Form ADV through the IARD using the same process used by registered investment advisers. An exempt reporting adviser must submit its initial Form ADV within 60 days of relying on the private funds adviser exemption or venture capital funds adviser exemption. Such information must be updated at least annually, within 90 days of the end of the adviser's fiscal year, and more frequently if required by the instructions to Form ADV.

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