Simpson Thacher

Memorandum

SEC Proposes Amendments to Form ADV and Certain Investment Advisers Act Rules

June 9, 2015

On May 20, 2015, the Securities and Exchange Commission (the "SEC") proposed amendments to Part 1A of Form ADV and certain rules under the U.S. Investment Advisers Act of 1940, as amended (the "Advisers Act"), in an effort to enhance the "quality of information available to investors" and to permit the SEC to "more effectively collect and use data provided" by investment advisers.[1]

With regard to Part 1A of Form ADV, the SEC has proposed (1) amendments that require an investment adviser of separately managed accounts ("SMAs")[2] to provide certain aggregate information on such SMAs, including the regulatory assets under management attributable to such SMAs ("SMA RAUM"), the asset categories in which they invest and their use of derivatives and borrowing, (2) amendments to expressly provide for "umbrella registration" for private fund advisers that together operate a single advisory business and (3) certain clarifying, technical and other amendments to existing items and instructions. The SEC has noted that the additional data collected by means of such Form ADV amendments would assist the SEC in preparing for, conducting and implementing the SEC's risk-based examination program of investment advisers, conducting investigations and bringing enforcement actions.[3]

Additionally, the SEC proposed amendments to the Advisers Act books and records rule, Rule 204-2, that

[1] *SEC Proposes Rules to Modernize and Enhance Information Reported by Investment Companies and Investment Advisers* (May 20, 2015), available at http://www.sec.gov/news/pressrelease/2015-95.html.

[2] According to the Proposing Release, for purposes of reporting on Form ADV, SMAs are "advisory accounts other than those that are pooled investment vehicles (*i.e.*, registered investment companies, business development companies, and pooled investment vehicles that are not investment companies (*i.e.*, private funds))." Amendments to Form ADV and Investment Advisers Act Rules, SEC Release No. IA-4091 (May 20, 2015) (the "Proposing Release"), at 8. While the plain meaning of the term SMA would suggest an account for a single client, the definition proposed by the SEC in the Proposing Release calls into question whether other collective investment schemes that are not "private funds" are captured within the term SMA.

[3] Proposing Release, at 4.

would require investment advisers to maintain additional records to support performance calculations and records of communications related to performance.

Proposed Amendments to Form ADV

Separately Managed Accounts

The SEC proposed to collect more specific information about the SMAs managed by investment advisers in Item 5 of Part 1A and Section 5 of Schedule D, including the:

- Approximate percentage of SMA RAUM invested in each of ten broad asset categories (consistent with categories used on Form PF);
- Number of SMAs that correspond to certain categories of gross notional exposure;
- Weighted average amount of borrowings[4] (as a percentage of net asset value) in SMAs; and
- Identity of any custodians that account for at least 10% of an investment adviser's SMA RAUM and the amount of the investment adviser's SMA RAUM held at the custodian.

Moreover, investment advisers with SMA RAUMs of at least $10 billion would be required to report:

- Weighted average gross notional value of derivatives (as a percentage of net asset value) in each of six different categories; and
- Both mid-year and year-end data regarding borrowings and derivatives in the investment adviser's annual updating amendment.

Umbrella Registration

The SEC's proposed amendments to Form ADV would also incorporate the concept of an "umbrella registration," being available where multiple private fund advisers conduct a single advisory business, thereby codifying the guidance provided in the 2012 SEC No-Action Letter provided to the American Bar Association (the "2012 ABA NAL").[5] The amended Form ADV General Instructions would set forth the conditions[6] for umbrella registration, which are the same as those in the 2012 ABA NAL (except that the

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[4] "The Glossary to Proposed Form ADV defines 'borrowings' as '[S]ecured borrowings and unsecured borrowings, collectively. Secured borrowings are obligations for borrowed money in respect of which the borrower has posted collateral or other credit support and should include any reverse repos (*i.e.*, any sale of securities coupled with an agreement to repurchase the same (or similar) securities at a later date at an agreed price). Unsecured borrowings are obligations for borrowed money in respect of which the borrower has not posted collateral or other credit support.' Proposing Release, at note 17.

[5] *See* American Bar Association, Business Law Section, SEC Staff Letter (Jan. 18, 2012), *available at* http://www.sec.gov/divisions/investment/noaction/2012/aba011812.htm.

[6] Such conditions for umbrella registration include:

- The filing adviser and each relying adviser advise only private funds and clients in SMAs that are qualified clients (as defined in Rule 205-3 under the Advisers Act) and are otherwise eligible to invest in the private funds advised by the filing adviser or a relying adviser and whose accounts pursue investment objectives and strategies that are

2012 ABA NAL also included Form ADV disclosure conditions, the substance of which is otherwise covered by the proposed amendments to Form ADV).

Although umbrella registration has been available since the issuance of the 2012 ABA NAL, Form ADV was not designed for such umbrella registration, leading to confusion for private fund advisers and the public and complicating the SEC's data collection and analysis on umbrella registrants. The SEC believes that the inclusion of more uniform filing requirements for umbrella registration in Form ADV will provide more consistent data about groups of private fund advisers that operate a single business by aggregating Form ADV data for each legal entity registered under the umbrella. This would, the SEC stated, also allow for greater comparability across private fund advisers.[7]

In addition, private fund advisers would be required to file a new "Schedule R" for each relying adviser, which would call for certain identifying information, the basis for registration and ownership information about the relying adviser. Although collecting such additional information for relying advisers and completing the revised Form ADV may be burdensome for private fund advisers at first, for the same reasons as those stated above, we believe that uniformity in the provision of information regarding relying advisers will be beneficial for private fund advisers and the public in the long-run.

The SEC stated in the Proposing Release that "umbrella registration" is not available to exempt reporting advisers ("ERAs"),[8] as the conditions of a single advisory business are defined partly to reflect requirements that only apply to registered investment advisers. We believe that some ERAs have been utilizing "umbrella registration" and should consider whether they need to instead file separate Form ADVs for each of their adviser entities.

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substantially similar or otherwise related to those private funds;
- The filing adviser has its principal office and place of business in the U.S. and, therefore, all substantive provisions of the Advisers Act and the rules thereunder apply to the filing adviser's and each relying adviser's dealings with each of its clients, regardless of whether any client or the filing adviser or relying adviser providing the advice is a U.S. person;
- Each relying adviser, its employees and the persons acting on its behalf are subject to the filing adviser's supervision and control and each relying adviser, its employees and the persons acting on its behalf are "persons associated with" the filing adviser (as defined in section 202(a)(17) of the Advisers Act);
- The advisory activities of each relying adviser are subject to the Advisers Act and the rules thereunder, and each relying adviser is subject to examination by the SEC; and
- The filing adviser and each relying adviser operate under a single code of ethics adopted in accordance with Rule 204A-1 under the Advisers Act and single set of written policies and procedures adopted and implemented in accordance with Rule 206(4)-(7) under the Advisers Act and administered by a single chief compliance officer in accordance with that rule.

Proposing Release, at 29-31.

[7] Proposing Release, at 28-29.

[8] ERAs (that are not also registering with any state securities authority) must complete only certain items of Form ADV Part 1A as well as corresponding schedules. The requirements in Form ADV Part 2 do not apply to ERAs. Form ADV: General Instructions #3, at 2-3.

Additional Information Regarding Investment Advisers and their Advisory Businesses and Affiliates

In addition to the above, the SEC proposed amendments to existing questions on Form ADV, which would require investment advisers to provide additional identifying information and information about their advisory businesses and affiliations. Such amendments would require an investment adviser to report, for example:

- The social media addresses of its social media platforms, such as Twitter, Facebook and LinkedIn, in addition to the investment adviser's website address (*Part 1A Item 1.I; Section 1.I of Schedule D*);
- Information about its offices other than its principal office and place of business, including the total number of offices at which it conducts its investment advisory business, its 25 largest offices in terms of number of employees (rather than its 5 largest offices in terms of number of employees as currently required), the number of employees who perform advisory functions from each office, the business activities conducted from each office and any other investment-related business conducted from each office (*Part 1A Item 1.F; Section 1.F of Schedule D*);
- Whether its chief compliance officer is compensated or employed by any other person for providing chief compliance officer services, and, if so, the name and IRS Employer Identification Number of that other person (*Part 1A Item 1.J*);
- Its own assets within a range (*Part 1A Item 1.O*);
- Number of clients and amount of its RAUM attributable to each category of clients as of the date it determines its RAUM (*Part 1A Item 5.D*);
- Approximate amount of RAUM that is attributable to non-U.S. clients (*Part 1A Item 5.F*);
- RAUM of all parallel managed accounts related to a registered investment company or business development company that it advises (*Part 1A Section 5.G.(3) of Schedule D*);
- Total RAUM attributable to acting as sponsor and/or portfolio manager of a wrap fee program (*Part 1A Item 5.I*); and
- The percentage of a private fund owned by qualified clients, as defined in Rule 205-3 under the Advisers Act (*Part 1A Section 7.B.(1) of Schedule D*).

Proposed Amendments to the Advisers Act Rules

Finally, the SEC proposed two amendments to the Advisers Act books and records rule, Rule 204-2 under the Advisers Act, that would require an investment adviser to maintain additional materials related to the calculation and distribution of performance information.

Rule 204-2(a)(16) under the Advisers Act currently requires registered investment advisers to maintain records supporting performance claims in communications that are distributed or circulated to ten or more

persons. The SEC is proposing to remove the "ten or more persons" condition and to replace it with "any person." Thus, investment advisers would be required to maintain the materials listed in Rule 204-2(a)(16) that demonstrate the calculation of the performance or rate of return of any communication that the investment adviser circulates or distributes, directly or indirectly, to any person.

Moreover, Rule 204-2(a)(7) currently requires that registered investment advisers maintain written communications received and copies of written communications sent by such investment advisers relating to "(i) any recommendation made or proposed to be made and any advice given or proposed to be given, (ii) any receipt, disbursement or delivery of funds or securities, or (iii) the placing or execution of any order to purchase or sell any security." The SEC proposes to require investment advisers also to maintain originals of all written communications received and copies of written communications sent by an investment adviser relating to the performance or rate of return of any or all managed accounts or securities recommendations.

Comments on the proposed amendments must be submitted to the SEC no later than 60 days after the publication of the proposed amendments in the Federal Register.

Please contact Lisa Klar (lisa.klar@stblaw.com; +1-212-455-3635) or the partner in the Private Funds Group with whom you work if you have any questions.

Simpson Thacher Worldwide

UNITED STATES

New York
425 Lexington Avenue
New York, NY 10017
+1-212-455-2000

Houston
600 Travis Street, Suite 5400
Houston, TX 77002
+1-713-821-5650

Los Angeles
1999 Avenue of the Stars
Los Angeles, CA 90067
+1-310-407-7500

Palo Alto
2475 Hanover Street
Palo Alto, CA 94304
+1-650-251-5000

Washington, D.C.
1155 F Street, N.W.
Washington, D.C. 20004
+1-202-636-5500

EUROPE

London
CityPoint
One Ropemaker Street
London EC2Y 9HU
England
+44-(0)20-7275-6500

ASIA

Beijing
3919 China World Tower
1 Jian Guo Men Wai Avenue
Beijing 100004
China
+86-10-5965-2999

Hong Kong
ICBC Tower
3 Garden Road, Central
Hong Kong
+852-2514-7600

Seoul
West Tower, Mirae Asset Center 1
26 Eulji-ro 5-gil, Jung-gu
Seoul 100-210
Korea
+82-2-6030-3800

Tokyo
Ark Hills Sengokuyama Mori Tower
9-10, Roppongi 1-Chome
Minato-Ku, Tokyo 106-0032
Japan
+81-3-5562-6200

SOUTH AMERICA

São Paulo
Av. Presidente Juscelino Kubitschek, 1455
São Paulo, SP 04543-011
Brazil
+55-11-3546-1000