

DODD-FRANK'S IMPACT ON INVESTMENT ADVISER REGISTRATION

Introduction

President Obama signed the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank") into law on July 21, 2010. Dodd-Frank will have a widespread effect across the financial services sector. The focus of this alert is on Dodd-Frank's impact on the registration requirements under the Investment Advisers Act of 1940 (the "Advisers Act"). Compliance with these provisions of Dodd-Frank is required no later than one year after the law is enacted.

SEC Threshold Increase

Each investment adviser that is currently registered with the United States Securities and Exchange Commission ("SEC") and that has assets under management in an amount that is less than \$100,000,000 will likely need to withdraw their SEC registration and register with one or more state securities administrators. While the Form ADV remains the vehicle that the adviser will use to apply for state registration, many state securities administrators impose additional application requirements that vary from state to state. We are not aware that any such state securities administrator has reduced the application requirements for SEC registrants transitioning to state registration as a result of Dodd-Frank. Nor are we aware of any basis for current SEC registrants to simply transition their existing state notice filings to full state registrations without completing the entire application package for each state where they are required to register. What we have been told is that one of the reasons for increasing the threshold was to alleviate the examination and enforcement burden on the SEC arising from mid-size advisers so that the SEC's resources can be allocated to matters that involve larger advisers. Therefore, we anticipate that the frequency and number of regulatory examinations by state securities administrators will increase.

From a practical standpoint, each SEC-registered investment adviser with assets under management below \$100,000,000, should:

- determine those states with which it must register as a state adviser and then apply for state registration in all such states.
- revise its marketing materials and website content to remove any reference to being an SEC or "federal" investment adviser.
- review all contracts (including vendor and client) for clauses that contain covenants or other provisions that require that the adviser maintain an effective SEC registration.
- discuss with each broker-dealer and custodian whether a transition to state registration will impact the services that the adviser receives.



- address with each provider of errors and omissions insurance whether a transition to state registration will reduce the dollar amount that the adviser pays for policy premiums.

Removal of “Private Adviser” Exemption

Prior to Dodd-Frank, many advisers to private equity and hedge funds relied on an exemption from investment adviser registration that was available for any adviser (1) who did not hold itself out generally to the public as an adviser, (2) did not advise any registered investment company or business development company, and (3) advised fewer than fifteen (15) clients during the course of the preceding twelve-month period. Advisers to private equity and hedge funds will now need to register with the SEC as investment advisers and comply with the provisions of the Advisers Act. In addition, each such adviser will have expanded reporting requirements that are expected to require them to disclose various business issues, including the adviser’s use of leverage, counterparty credit risk exposure, valuation policies, and type and amount of assets held.

From a practical standpoint, each adviser to private equity and/or hedge funds should:

- determine whether it must register as an investment adviser with the SEC or with one or more state securities administrators.
- review the offering materials for the fund(s) that it advises to remove any references to the adviser operating under or relying on the “private adviser exemption” from Advisers Act registration.
- revise fund offering materials to disclose that the fund’s adviser may be required to disclose to the SEC certain details of its operations and business practices, and that the adviser may be subject to regulatory audit by the SEC.
- disclose to fund investors that the fund’s adviser may be legally compelled to share information concerning the fund and the fund’s investors to governmental authorities.

Venture Capital and Smaller Private Fund Adviser Exemption

Investment adviser registration will not be required for advisers:

- (1) of one or more private funds, each of which has less than \$150,000,000 in assets under management; or
- (2) to venture capital funds.

Although registration will not be required for advisers that rely upon these exemptions, they must satisfy certain reporting requirements as directed by the SEC. In addition, they must comply with the anti-fraud provisions of the Advisers Act.

As a practical matter, each adviser that relies on one of the above exemptions from registration should retain evidence (on an initial and ongoing basis) that corroborates that it satisfies the applicable exemption.



Family Office Exemption

Historically, the SEC has provided no-action assurance to family offices from the registration requirements of the Advisers Act. As a result of Dodd-Frank, the SEC will formally define the term “family office,” and each adviser that meets that definition will be exempt from investment adviser registration. Nonetheless, each family office will need to maintain compliance with the anti-fraud provisions of the Advisers Act. Similar to those advisers relying upon other exemptions from Advisers Act registration, each adviser that relies on the “family office” exemption should retain evidence (on an initial and ongoing basis) that corroborates that it satisfies the requirements of the exemption.

Foreign Private Adviser Exemption

Foreign private advisers would be exempt from investment adviser registration. A foreign private adviser relying on this exemption must be one who (1) has no place of business in the United States, (2) has, in total, fewer than fifteen (15) clients and investors in the United States in private funds advised by the investment adviser, (3) has aggregate assets under management from United States clients and United States investors in private funds advised by the adviser of less than \$25,000,000 (or such higher amount as the SEC may, by rule, deem appropriate), and (4) neither (a) holds itself out generally to the public in the United States as an investment adviser nor (b) acts as an investment adviser to any investment company or business development company. We expect that foreign private advisers will need to maintain compliance with the anti-fraud provisions of the Advisers Act. Notwithstanding the foregoing, each foreign private adviser is subject to the rules and regulations that are promulgated by the securities administrator that governs their “home” jurisdiction. Therefore, while an adviser may be exempt from SEC registration, they may be required to register with the securities administrator of the countries in which they do business.

Throughout the next twelve (12) months, the SEC will interpret Dodd-Frank and issue new rules to address the provisions of Dodd-Frank, including those that are set forth above. We remain available to assist with analyzing those rules and determining the impact that they may have on you and your business.

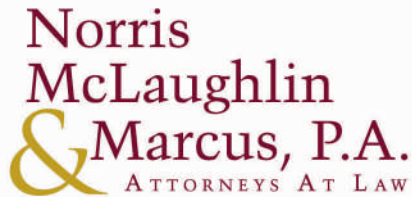
This *Securities Law Alert* was written by **Oren M. Chaplin, Esq.**, an attorney with Norris McLaughlin & Marcus, P.A. If you have any question about any information contained in this alert or any other questions related to securities law, please do not hesitate to contact Oren, by phone at (908) 252-4282 or by email at omchaplin@nmmlaw.com.

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About the Securities Law Group

The Securities Law Group at Norris McLaughlin & Marcus is experienced in dealing with both federal and state securities law matters. We represent clients attempting to raise investment capital from private placements and venture capital deals to registered firm commitment underwritten offerings of securities. Our experience with securities registration also includes matters ranging from stock option plans to dividend reinvestment plans. Our attorneys are well acquainted with SEC Rules 144 and 145 and frequently deal with the resale of unregistered stock by executives and the impact of the securities laws on merger transactions. We regularly represent public companies in dealing with compliance and anti-fraud issues under the Securities Exchange Act of 1934, as amended, including (i) proxy statements, (ii) periodic reports (Form 10-K and 10-Q), and (iii) inside stock trading and compensation plans (Form 3, 4 and 5 and the rules under Section 16[b]). We have also advised a number of public clients on available takeover defenses, including supermajority voting requirements and "poison pills" and are acquainted with the Williams Act provision of the 1934 Act.

In addition to our experience with public companies, the attorneys in our Securities Law Group regularly represent businesses and individuals involved in the financial services sector, including financial planning firms, investment advisers, broker-dealers, public and private accounting firms, hedge and other private equity funds, and banking and thrift institutions. We counsel our clients on formation, corporate governance, employment, and regulatory issues under both state and federal securities laws in connection with establishing and operating their businesses. Our attorneys are regularly involved with analyzing and resolving issues that arise under the Investment Advisers Act of 1940, Securities Exchange Act of 1934, Securities Act of 1933, ERISA, Investment Company Act of 1940, and state blue sky laws, and frequently interact with the SEC, Department of Labor, FINRA and state securities administrators in connection with examinations, inquiries, investigations and other proceedings.



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