COMMODITY FUTURES TRADING COMMISSION

17 CFR Part 4

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SECURITIES AND EXCHANGE COMMISSION

17 CFR Parts 275 and 279

Release No. IA-3308; File No. S7-05-11

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Reporting by Investment Advisers to Private Funds and Certain Commodity Pool Operators and Commodity Trading Advisors on Form PF

AGENCIES: Commodity Futures Trading Commission and Securities and Exchange Commission.

ACTION: Joint final rules.

SUMMARY: The Commodity Futures Trading Commission ("CFTC") and the Securities and Exchange Commission ("SEC") (collectively, "we" or the "Commissions") are adopting new rules under the Commodity Exchange Act and the Investment Advisers Act of 1940 to implement provisions of Title IV of the Dodd-Frank Wall Street Reform and Consumer Protection Act. The new SEC rule requires investment advisers registered with the SEC that advise one or more private funds and have at least $150 million in private fund assets under management to file Form PF with the SEC. The new CFTC rule requires commodity pool operators ("CPOs") and commodity trading advisors ("CTAs") registered with the CFTC to satisfy certain CFTC filing requirements with respect to private funds, should the CFTC adopt such requirements, by filing Form PF with the SEC, but only if those CPOs and CTAs are also registered with the SEC as investment advisers and are required to file Form PF under the

Advisers Act. The new CFTC rule also allows such CPOs and CTAs to satisfy certain CFTC filing requirements with respect to commodity pools that are not private funds, should the CFTC adopt such requirements, by filing Form PF with the SEC. Advisers must file Form PF electronically, on a confidential basis. The information contained in Form PF is designed, among other things, to assist the Financial Stability Oversight Council in its assessment of systemic risk in the U.S. financial system.

DATES: See section III of this Release.

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SUPPLEMENTARY INFORMATION: The CFTC is adopting rule 4.27 [17 CFR 4.27] under the Commodity Exchange Act ("CEA")[1] and Form PF.[2] The SEC is

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1 7 U.S.C. 1a.

2 Form PF is a joint form between the SEC and the CFTC only with respect to sections 1 and 2 of the Form. Sections 3 and 4 of the Form are adopted solely by the SEC.

adopting rule 204(b)-1 [17 CFR 275.204(b)-1] and Form PF [17 CFR 279.9] under the Investment Advisers Act of 1940 [15 U.S.C. 80b] ("Advisers Act").[3]

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[3] 15 U.S.C. 80b. Unless otherwise noted, when we refer to the Advisers Act, or any paragraph of the Advisers Act, we are referring to 15 U.S.C. 80b of the United States Code, at which the Advisers Act is codified, and when we refer to Advisers Act rule 204(b)-1, or any paragraph of this rule, we are referring to 17 CFR 275.204(b)-1 of the Code of Federal Regulations in which this rule will be published. In addition, when we refer to the "Investment Company Act," or any paragraph of the Investment Company Act, we are referring to 15 U.S.C. 80a of the United States Code, at which the Investment Company Act of 1940 is codified.

I. BACKGROUND

A. The Dodd-Frank Act and the Financial Stability Oversight Council

On July 21, 2010, President Obama signed into law the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act").[4] One significant focus of this legislation is to "promote the financial stability of the United States" by, among other measures, establishing better monitoring of emerging risks using a system-wide perspective.[5] To further this goal, the Act establishes the Financial Stability Oversight Council ("FSOC") and directs it to monitor risks to the U.S. financial system. The Act

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4 Pub. L. No. 111-203, 124 Stat. 1376 (2010).

5 S. REP. NO. 111-176, at 2-3 (2010) ("Senate Committee Report").

also gives FSOC a number of tools to carry out this mission.[6] For instance, FSOC may determine that a nonbank financial company will be subject to the supervision of the Board of Governors of the Federal Reserve System ("FRB") if the company may pose risks to U.S. financial stability as a result of its activities or in the event of its material financial distress.[7] In addition, FSOC may issue recommendations to primary financial regulators, like the SEC and CFTC, for more stringent regulation of financial activities that FSOC determines may create or increase systemic risk.[8]

The Dodd-Frank Act anticipates that various regulatory agencies, including the Commissions, will support FSOC.[9] To that end, the Dodd-Frank Act amended section 204(b) of the Advisers Act to require that the SEC establish reporting and recordkeeping requirements for advisers to private funds,[10] many of which must also

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6 *See* Sections 113 and 120 of the Dodd-Frank Act. In a recent rulemaking release, FSOC explained that its response to any potential threat to financial stability will be based on an assessment of the circumstances. *See Authority to Require Supervision and Regulation of Certain Nonbank Financial Companies*, Financial Stability Oversight Counsel Release (Oct. 11, 2011) ("FSOC Second Notice").

7 Section 113 of the Dodd-Frank Act. The Dodd-Frank Act also directs FSOC to recommend to the FRB heightened prudential standards for designated nonbank financial companies. Section 112(a)(2) of the Dodd-Frank Act.

8 Section 120 of the Dodd-Frank Act.

9 *See, e.g.*, section 112(d)(1) of the Dodd-Frank Act, which authorizes FSOC to collect information from member agencies to support its functions. *See also* FSOC Second Notice, *supra* note 6 (explaining that information reported on Form PF will be important to FSOC's policy-making in regard to the assessment of systemic risk among private fund advisers).

10 Section 202(a)(29) of the Advisers Act defines the term "private fund" as "an issuer that would be an investment company, as defined in section 3 of the Investment Company Act, but for section 3(c)(1) or 3(c)(7) of that Act." Section 3(c)(1) of the Investment Company Act provides an exclusion from the definition of "investment company" for any "issuer whose outstanding securities (other than short-term paper) are beneficially owned by not more than one hundred persons and which is not making and does not presently propose to make a public offering of its securities." Section 3(c)(7) of the Investment

register for the first time as a consequence of the Dodd-Frank Act.[11] These new requirements may include maintaining records and filing reports containing such information as the SEC deems necessary and appropriate in the public interest and for investor protection or for the assessment of systemic risk by FSOC.[12] The SEC and CFTC must jointly issue, after consultation with FSOC, rules establishing the form and content of any reports to be filed under this new authority.[13]

On January 26, 2011, in a joint release, the CFTC and SEC proposed new rules and a new reporting form intended to implement this statutory mandate.[14] In the release,

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Company Act provides an exclusion from the definition of "investment company" for any "issuer, the outstanding securities of which are owned exclusively by persons who, at the time of acquisition of such securities, are qualified purchasers, and which is not making and does not at that time propose to make a public offering of such securities." The term "qualified purchaser" is defined in section 2(a)(51) of the Investment Company Act.

11 *See* sections 402, 403, 407 and 408 of the Dodd-Frank Act. The SEC recently adopted rule 203-1(e) providing a transition period for certain private advisers previously relying on the repealed exemption in section 203(b)(3) of the Advisers Act. The transition rule requires these advisers to register with the SEC by March 30, 2012. *See Rules Implementing Amendments to the Investment Advisers Act of 1940*, Investment Advisers Act Release No. IA-3221 (June 22, 2011), 76 FR 42,950 (July 19, 2011) ("Implementing Adopting Release"). *See also Exemptions for Advisers to Venture Capital Funds, Private Fund Advisers With Less Than $150 Million in Assets Under Management, and Foreign Private Advisers*, Investment Advisers Act Release No. IA-3222 (June 22, 2011), 76 FR 39,646 (July 6, 2011) ("Exemptions Adopting Release").

12 The Dodd-Frank Act does not identify specific information to be included in these reports, but section 204(b) of the Advisers Act does require that the records and reports required under that section cumulatively include a description of certain information about private funds, such as the amount of assets under management, use of leverage, counterparty credit risk exposure, and trading and investment positions for each private fund advised by the adviser. *See Reporting by Investment Advisers to Private Funds and Certain Commodity Pool Operators and Commodity Trading Advisors on Form PF*, Investment Advisers Act Release No. 3145 (January 26, 2011), 76 FR 8,068 (February 11, 2011) ("Proposing Release") at n. 13 and accompanying text.

13 *See* section 211(e) of the Advisers Act.

14 As discussed below, Form PF is a joint form between the SEC and the CFTC only with respect to sections 1 and 2 of the Form.

the SEC proposed new Advisers Act rule 204(b)-1, which would require private fund advisers to file Form PF periodically with the SEC.[15] In addition, the CFTC proposed new rule 4.27,[16] which would require private fund advisers that are also registered as CPOs or CTAs with the CFTC to satisfy certain proposed CFTC systemic risk reporting requirements, should the CFTC adopt such requirements, by filing Form PF.[17] Today, we are adopting these proposed rules and Form PF with several changes from the proposal that are designed to respond to commenter concerns. Consistent with the proposal, advisers must report on Form PF certain information regarding the private

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15 Throughout this Release, we use the term "private fund adviser" to mean any investment adviser that (i) is registered or required to register with the SEC (including any investment adviser that is also registered or required to register with the CFTC as a CPO or CTA) and (ii) advises one or more private funds. Advisers solely to venture capital funds or advisers solely to private funds that in the aggregate have less than $150 million in assets under management in the United States that rely on the exemption from registration under, respectively, section 203(l) or 203(m) of the Advisers Act ("exempt reporting advisers") are not required to file Form PF. *See infra* section II.A.7 of this Release.

16 Because the CFTC is not adopting the remainder of proposed CEA rule 4.27 at the same time as it is adopting this rule, the CFTC has modified the designation of CEA rule 4.27(d) to be the sole text of that section. *See Commodity Pool Operators and Commodity Trading Advisors: Amendments to Compliance Obligations* (Jan. 26, 2011), 76 FR 7976 (Feb. 11, 2011) ("CFTC Proposing Release"). Additionally, the CFTC has made some revisions to the text of rule 4.27 to: (1) clarify that the filing of Form PF with the SEC will be considered substitute compliance with certain CFTC reporting obligations (*i.e.*, for Schedules B and C of Form CPO-PQR and Schedule B of Form CTA-PR as proposed) should the CFTC determine to adopt such requirements and (2) to allow CPOs and CTAs who are otherwise required to file Form PF the option of submitting on Form PF data regarding commodity pools that are not private funds as substitute compliance with certain CFTC reporting obligations (*i.e.*, for Schedules B and C of Form CPO-PQR and Schedule B of Form CTA-PR as proposed) should the CFTC determine to adopt such requirements.

17 For these private fund advisers, filing Form PF through the Form PF filing system would be a filing with both the SEC and CFTC. Irrespective of their filing a Form PF with the SEC, the CFTC has proposed that all private fund advisers that are also registered as CPOs and CTAs with the CFTC would be required to file Schedule A of Form CPO-PQR (for CPOs) or Schedule A of Form CTA-PR (for CTAs). *See* CFTC Proposing Release, *supra* note 16.

funds they manage, and this information is intended to complement information the SEC collects on Form ADV and information the CFTC separately has proposed to collect from CPOs and CTAs.[18] Collectively, these reporting forms will provide FSOC and the Commissions with important information about the basic operations and strategies of private funds and help establish a baseline picture of potential systemic risk in the private fund industry.

The SEC is adopting Advisers Act rule 204(b)-1 and Form PF to enable FSOC to obtain data that will facilitate monitoring of systemic risk in U.S. financial markets. Our understanding of the utility to FSOC of the data to be collected is based on our staffs' consultations with staff representing the members of FSOC. The design of Form PF is not intended to reflect a determination as to where systemic risk exists but rather to provide empirical data to FSOC with which it may make a determination about the extent to which the activities of private funds or their advisers pose such risk. The information made available to FSOC will be collected for FSOC's use by the Commissions in their role as the primary regulators of private fund advisers. 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.

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[18] *See* Proposing Release, *supra* note 12, at n. 16, comparing the purposes of Form ADV and Form PF. References in this Release to Form ADV or terms defined in Form ADV or its glossary are to the form and glossary as amended in the Implementing Adopting Release, *supra* note 11.

We expect the information collected on Form PF and provided to FSOC will be an important part of FSOC's systemic risk monitoring in the private fund industry.[19] We note that, simultaneous with the consultations between our staffs and the staff representing FSOC's members, FSOC has been building out its standards for assessing systemic risk across different kinds of financial firms and has proposed guidance and standards for determining which nonbank financial companies should be designated as subject to FRB supervision.[20] In its most recent release on this subject, FSOC confirmed that the information reported on Form PF is important not only to conducting an assessment of systemic risk among private fund advisers but also to determining how that assessment should be made.[21]

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[19] *See* section 204(b) of the Advisers Act. Today, regulators have little reliable data regarding this rapidly growing sector and frequently have to rely on data from other sources, which when available may be incomplete. *See*, *e.g.*, FSOC 2011 Annual Report, http://www.treasury.gov/initiatives/fsoc/Pages/annual-report.aspx ("FSOC 2011 Annual Report") at 69. The SEC recently adopted amendments to Form ADV that will require the reporting of important information regarding private funds, but this includes little or no information regarding, for instance, performance, leverage or the riskiness of a fund's financial activities. *See* Implementing Adopting Release, supra note 11. The data collected through Form PF will be more reliable than existing data regarding the industry and significantly extend the data available through the revised Form ADV.

[20] *See*, *e.g.*, FSOC Second Notice, *supra* note 6; *Authority to Require Supervision and Regulation of Certain Nonbank Financial Companies*, Financial Stability Oversight Council Release (Jan. 18, 2011), 76 FR 4,555 (Jan. 26, 2011); *Advance Notice of Proposed Rulemaking Regarding Authority to Require Supervision and Regulation of Certain Nonbank Financial Companies*, Financial Stability Oversight Council Release (Oct. 1, 2010), 75 FR 61,653 (Oct. 6, 2010).

[21] *See* FSOC Second Notice, *supra* note 6 ("[FSOC] recognizes that the quantitative thresholds it has identified for application during [the initial stage of review] may not provide an appropriate means to identify a subset of nonbank financial companies for further review in all cases across all financial industries and firms. While [FSOC] will apply [such] thresholds to all nonbank financial companies, including... asset management companies, private equity firms, and hedge funds, these companies may pose risks that are not well-measured by the quantitative thresholds approach.... Using [Form PF] and other data, [FSOC] will consider whether to establish an additional set of

The Commissions received more than 35 letters responding to the proposal, with trade associations, investment advisers and law firms accounting for most of the comments. Commenters representing investors were generally supportive of the proposal but thought it should have required more of private fund advisers.[22] Some of these supporters argued, in particular, for more detailed and more frequent reporting than we proposed.[23] In contrast, advisers and those writing on their behalf expressed concern regarding the scope, frequency and timing of the proposed reporting.[24] A number of these commenters generally supported the systemic risk monitoring goals of the Dodd-Frank Act or the broad framework of the proposal but argued that specific aspects of the

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metrics and thresholds tailored to evaluate hedge funds and private equity firms and their advisers.").

22 *See, e.g.*, comment letter of the American Federation of Labor and Congress of Industrial Organizations (Apr. 12, 2011) ("AFL-CIO Letter"); comment letter of the Council of Institutional Investors (Apr. 11, 2011) ("CII Letter") (agreeing that "the SEC's proposal will facilitate FSOC's ability to promote the soundness of the U.S. financial system" but noting that the commenter's own working group report favored real-time reporting of position-level information).

23 *See* AFL-CIO Letter ("We support the Proposed Rule, but believe it should be strengthened in a few key areas by requiring more frequent reporting, omitting the arbitrary distinction by investment strategy, and adding additional disclosure requirements necessary to protect investors and prevent systemic risks."); comment letter of the Americans for Financial Reform (Apr. 12, 2011) ("AFR Letter") (endorsing the AFL-CIO Letter).

24 *See, e.g.*, comment letter of the Alternative Investment Management Association (Apr. 12, 2011) ("AIMA General Letter"); comment letter of the Investment Adviser Association (Apr. 12, 2011) ("IAA Letter"); comment letter of the Managed Funds Association (Apr. 8, 2011) ("MFA Letter"); comment letter of the Private Equity Growth Capital Council (Apr. 12, 2011) ("PEGCC Letter"); comment letter of Seward & Kissel, LLP (Apr. 12, 2011) ("Seward Letter"); comment letter of the Securities Industry and Financial Markets Association, Asset Management Group (Apr. 12, 2011) ("SIFMA Letter").

proposal were impractical or burdensome.[25] We respond to these comments in section II of this Release.

This rulemaking is intended primarily to support FSOC, consistent with the mandate to adopt private fund reporting requirements under the Dodd-Frank Act. Determinations made with respect to the Form PF reporting requirements have been made in furtherance of this goal and to comply with this legislative mandate.

B. International Coordination

The Dodd-Frank Act states that FSOC shall coordinate with foreign financial regulators in assessing systemic risk.[26] In recognition of this, our proposal discussed the potential importance of international regulatory coordination in responding to future financial crises.[27] A number of groups have continued to advance international efforts relating to the collection of systemic risk information. For example, recent reports from the Financial Stability Board ("FSB"), International Monetary Fund ("IMF") and Bank for International Settlements ("BIS") emphasize the importance of identifying and

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25 *See, e.g.*, comment letter of BlackRock Inc. (Apr. 12, 2011) ("BlackRock Letter"); IAA Letter (stating that they "fully support the Commission's goal of enhancing transparency of private funds that may be deemed to present systemic risk to the U.S. financial markets" but arguing that the proposal is too broad in scope); MFA Letter (supporting "the approach proposed by the SEC and CFTC to collect information from registered private fund managers through periodic, confidential reports on Form PF" and stating that the collection of data from market participants, including investment advisers and the funds they manage, "is a critical component of effective systemic risk monitoring and regulation").

26 *See* section 175(b) of the Dodd-Frank Act. *See also* Proposing Release, *supra* note 12, at nn. 19-22 and accompanying text.

27 *See* Proposing Release, *supra* note 12, at section I.B.

addressing gaps in the information available to systemic risk regulators.[28] One goal of this coordination is to collect comparable information regarding private funds, which will aid in the assessment of systemic risk on a global basis.[29] Several commenters agreed that international coordination in connection with private fund reporting is important and encouraged us to take an approach consistent with international precedents.[30]

To this end, our staffs have consulted with the United Kingdom's Financial Services Authority (the "FSA"), the European Securities and Markets Authority ("ESMA"), the International Organization of Securities Commissions ("IOSCO") and Hong Kong's Securities and Futures Commission.[31] The FSA was the first to develop significant experience with hedge fund reporting, conducting a voluntary, semi-annual survey beginning in October 2009 by sampling large hedge fund groups based in the

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28 *See, e.g.*, FSB, IMF and BIS, *Macroprudential Policy Tools and Frameworks, Update to G20 Finance Ministers and Central Bank Governors* (Feb. 14, 2011) (highlighting the need for "[d]esign and collection of better information and data to support systemic risk identification and modelling [sic]"); FSB, *Shadow Banking: Scoping the Issues, A Background Note of the Financial Stability Board* (Apr. 12, 2011) ("FSB Shadow Banking Report") ("authorities should cast the net wide, looking at all non-bank credit intermediation to ensure that data gathering and surveillance cover all the activities within which shadow banking-related risks might arise"); FSB and IMF, *The Financial Crisis and Information Gaps, Implementation Progress Report* (June 2011) ("Report on Information Gaps").

29 *See, e.g.*, Report on Information Gaps, *supra* note 28, at 5. The Commissions expect that they may share information reported on Form PF with various foreign financial regulators under information sharing agreements in which the foreign regulator agrees to keep the information confidential.

30 *See, e.g.*, comment letter of the American Bar Association, Federal Regulation of Securities Committee and Private Equity and Venture Capital Committee (Apr. 11, 2011) ("ABA Committees Letter"); AIMA General Letter; comment letter of the Committee on Capital Markets Regulation (Apr. 12, 2011) ("CCMR Letter").

31 These consultations began prior to issuance of the Form PF proposal and have continued during the development of the final rules and Form. *See also* Proposing Release, *supra* note 12, at nn. 24-32 and accompanying text.

United Kingdom.[32] IOSCO, in turn, used the guidelines established in the FSA Survey, together with its own report on hedge fund oversight, in coordinating a survey of hedge funds conducted by IOSCO's members (including the SEC and CFTC) as of the end of September 2010.

Most recently, ESMA has proposed its own template for private fund reporting, which shares many common elements with the FSA Survey (as well as the IOSCO survey and Form PF).[33] ESMA's proposed template will serve as the basis for mandatory private fund reporting in Europe under the European Union's Directive on alternative investment fund managers ("EU Directive") and is expected eventually to supersede the FSA Survey in the United Kingdom. The proposed ESMA template is broader in scope than the FSA Survey, requiring information about a wide range of alternative investment funds, including private equity funds, venture capital funds and real estate funds.[34] Form PF includes many of the types of information collected through the FSA Survey and proposed to be collected in the ESMA template, and a number of the changes we are

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32 *See, e.g.*, Financial Services Authority, *Assessing the Possible Sources of Systemic Risk from Hedge Funds: A Report on the Findings of the Hedge Fund Survey and the Hedge Fund as Counterparty Survey* (July 2011), *available at http://www.fsa.gov.uk/pubs/other/hedge_fund_report_july2011.pdf* ("FSA Survey"). *See also* Proposing Release, *supra* note 12, at nn. 27-30 and accompanying text.

33 *See ESMA's draft technical advice to the European Commission on possible implementing measures of the Alternative Investment Fund Managers Directive*, ESMA/2011/209 (July 2011), available at http://www.esma.europa.eu/index.php?page=consultation_details&id=185 ("ESMA Proposal"). *See also* Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EU and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010 (published July 1, 2011, in the Official Journal of the European Union).

34 For additional discussion of international efforts relating to systemic risk monitoring in private equity funds, *see* Proposing Release, *supra* note 12, at nn. 33-35 and accompanying text.

making from the proposal further align Form PF with these international approaches to private fund reporting.[35]

II. DISCUSSION

The SEC is adopting Form PF and rule 204(b)-1 under the Advisers Act with several changes from the proposal that are designed to respond to commenter concerns. Under the new rule, SEC-registered investment advisers must report systemic risk information to the SEC on Form PF if they advise one or more private funds.[36] The final rule and changes from the proposal are discussed below.[37]

In addition, the CFTC is adopting rule 4.27 with minor revisions.[38] This new rule provides that, for registered CPOs and CTAs that are also registered as investment advisers with the SEC and are required to file Form PF, filing Form PF serves as substitute compliance for certain of the CFTC's proposed systemic risk reporting requirements should the CFTC adopt such requirements.[39] The CFTC has revised the

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35 *See*, *e.g.*, *infra* notes 227, 231, 244-246, 258, 279, 283 and 297 and accompanying text.

36 *See* Advisers Act rule 204(b)-1.

37 As noted above, section 204(b) of the Advisers Act gives the SEC authority to establish both reporting and recordkeeping requirements for private fund advisers. *See supra* note 12 and accompanying text. One commenter asked why the SEC proposed reporting requirements before proposing recordkeeping requirements for private fund advisers, expressing concern that advisers would need to know what records to maintain in order to report on Form PF. *See* comment letter of Congressman Darrell E. Issa, Chairman of the House Committee on Oversight and Government Reform (Sept. 20, 2011) ("Issa Letter"). Recordkeeping requirements serve a number of important purposes, such as ensuring that advisers maintain adequate documentation relevant to the disposition of their clients' and investors' assets and that SEC examiners are able to effectively inspect advisers' operations. The SEC does not believe, however, that establishing recordkeeping requirements is a necessary prerequisite to establishing reporting requirements.

38 *See supra* note 16.

39 *See* CEA rule 4.27. For purposes of this rule, it is the CFTC's position that any false or misleading statement of a material fact or material omission in the jointly adopted

new rule to allow CPOs and CTAs who are otherwise required to file Form PF the option of submitting on Form PF data regarding commodity pools that are not private funds as substitute compliance with certain of the CFTC's proposed systemic risk reporting requirements should the CFTC adopt such requirements.[40] The CFTC believes that the revisions to the CEA rule adopted in this Release provide additional clarity with respect to the filing obligations of dually registered CPOs and CTAs. Because commodity pools that are reported or required to be reported on Form PF are categorized as hedge funds for purposes of Form PF, as discussed below, CPOs and CTAs filing Form PF need to complete only the sections applicable to hedge fund advisers.[41]

As discussed above and in the Proposing Release, we have designed Form PF, in consultation with staff representing FSOC's members, to provide FSOC with information important to its understanding and monitoring of systemic risk in the private fund industry.[42] Based on our staffs' consultations with staff representing FSOC's members, we expect that FSOC will use the information collected on Form PF, together with market data from other sources, to assist in determining whether and how to deploy its regulatory tools. This may include, for instance, identifying private funds that merit further analysis or deciding whether to recommend to a primary financial regulator, like

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sections (sections 1 and 2) of Form PF that is filed by these CPOs and CTAs shall constitute a violation of section 6(c)(2) of the CEA.

40 *Id.*

41 Form PF is a joint form between the SEC and the CFTC only with respect to sections 1 and 2 of the Form. Accordingly, private fund advisers that are also CPOs or CTAs would be obligated to complete only section 1 and, if they meet the applicable threshold, section 2 of Form PF.

42 *See* Proposing Release, *supra* note 12, at section II.A and at n. 49.

the SEC or CFTC, more stringent regulation of the financial activities of the private fund industry.[43]

Although the Form we are adopting will provide information useful to FSOC's regulatory mission, the Form has not been designed to be FSOC's exclusive source of information regarding the private fund industry.[44] FSOC's recently proposed guidance regarding its process for designating nonbank financial companies that may pose risks to U.S. financial stability for FRB supervision helps to illustrate how FSOC may use the Form PF data along with other data sources.[45] This guidance would establish a three-stage process for determinations, at least in non-emergency situations. In the first and second stages, FSOC would screen firms using progressively more granular analyses of publicly available data and data that, like Form PF, are collected by other regulators. In the third stage, FSOC would work with the Office of Financial Research ("OFR") to conduct an in-depth review of specific firms identified in the first two stages, and this would generally involve OFR collecting additional, targeted information directly from these firms.[46] Similarly, in determining whether to exercise its other authorities for

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43 *See supra* note 6.

44 *See* Proposing Release, *supra* note 12, at n. 50 and accompanying text.

45 *See* FSOC Second Notice, *supra* note 6. *See also* section 113 of the Dodd-Frank Act for a discussion of the matters that FSOC must consider when determining whether a U.S. nonbank financial company will be supervised by the FRB and subject to prudential standards.

46 *See* sections 153 and 154 of the Dodd-Frank Act. One commenter expressed support for our approach, agreeing that, "Form PF should be used to obtain enough information to make a preliminary assessment, which can be followed up with data requests and dialogue for those firms who may potentially pose systemic risks – Form PF should not be considered the 'complete picture' of the private fund industry." AIMA General Letter.

addressing potential systemic risks, we expect that FSOC would likely utilize data from other sources in addition to Form PF.

Form PF is primarily intended to assist FSOC in its monitoring obligations under the Dodd-Frank Act, but the Commissions may use information collected on Form PF in their regulatory programs, including examinations, investigations and investor protection efforts relating to private fund advisers. In section VI.A of this Release, we discuss some of the ways in which the SEC could use proposed Form PF data for its regulatory activities and investor protection efforts.

As discussed in more detail below, the amount and type of information required on Form PF varies based on both the size of the adviser and the types of funds managed. For instance, Form PF requires more detailed information from advisers managing a large amount of hedge fund or liquidity fund assets than from advisers managing fewer assets or other types of funds. This scaled approach is intended to provide FSOC with a broad picture of the private fund industry while relieving smaller advisers from much of the detailed reporting.[47] Based on our staffs' consultations with staff representing FSOC's members, we understand that obtaining this broad picture will help FSOC to contextualize its analysis and assess whether systemic risk may exist across the private fund industry and to identify areas where OFR may want to obtain additional

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[47] In this Release, we refer to advisers that do not satisfy a Large Private Fund Adviser threshold as "smaller private fund advisers." This is not intended to imply that these advisers are small, only that they fall under certain of the Form's reporting thresholds. *See* section VI of this Release for a discussion of entities that are regarded as small for purposes of the Advisers Act.

information. This scaled approach is also designed to reflect the different implications for systemic risk that may be presented by different investment strategies.

A. Who Must File Form PF

An investment adviser must file Form PF if it: (1) is registered or required to register 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 its most recently completed fiscal year.[48] A CPO or CTA that is also registered or required to register with the SEC as an investment adviser and satisfies the other conditions described above must file Form PF with respect to any commodity pool it manages that is a "private fund" and may file Form PF with respect to any commodity pool it manages that is not a "private fund."[49] By filing Form PF with respect to these commodity pools, a CPO will be deemed to have satisfied certain filing requirements for these pools under the CFTC's regulatory regime should the CFTC adopt such requirements.[50]

We have modified the conditions under which an adviser must file Form PF by adding a minimum reporting threshold of $150 million in private fund assets under

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48 *See* Advisers Act rule 204(b)-1. This rule requires advisers to calculate the value of private fund assets under management pursuant to instructions in Form ADV, which provide a uniform method of calculating assets under management for regulatory purposes under the Advisers Act. *See* Implementing Adopting Release, *supra* note 11, at section II.A.3 (discussing the rationale underlying the new instructions for calculating assets under management for regulatory purposes).

49 *See supra* note 10 for the definition of "private fund."

50 *See* CEA rule 4.27. In the Proposing Release, the CFTC stated that a CPO registered with the CFTC that is also registered as a private fund adviser with the SEC will be deemed to have satisfied its filing requirements for Schedules B and C of Form CPO-PQR by completing and filing the applicable portions of Form PF for each of its commodity pools that satisfy the definition of "private fund" in the Dodd-Frank Act.

management.[51] Under the proposal, all private fund advisers registered with the SEC would have been required to file Form PF. The Dodd-Frank Act modified the Advisers Act's minimum registration requirements so that most advisers with less than $100 million in assets under management must register with one or more states rather than the SEC.[52] In addition, the Dodd-Frank Act created exemptions from SEC registration for advisers solely to venture capital funds and for advisers solely to private funds that in the aggregate have less than $150 million in assets under management in the United States.[53] As a result, under our proposed approach, most advisers with under $100 million in assets under management, and many advisers with less than $150 million in private fund assets under management, would not have reported on Form PF because they would not be registered with the SEC. However, some registered advisers with relatively few private fund assets would have been required to report on Form PF while exempt advisers with less than $150 million in private fund assets under management would not have been required to file Form PF.

Commenters argued that this outcome was not justified from a systemic risk perspective and recommended a minimum reporting threshold for advisers based on the amount of private fund assets under management.[54] One commenter proposed setting the

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51 *See* Advisers Act rule 204(b)-1.

52 *See* section 203A of the Advisers Act. *See also* Implementing Adopting Release, *supra* note 11, at section II.A.

53 *See* sections 203(l) and 203(m) of the Advisers Act and rules 203(l)-1 and 203(m)-1 under the Advisers Act. *See also* Exemptions Adopting Release, *supra* note 11.

54 *See, e.g.*, IAA Letter; Seward Letter. Two commenters also supported a minimum reporting threshold based on the size of individual funds, suggesting an exclusion for funds "with net asset values of less than $250 million and that are less than 5% of a manager's assets under management...." MFA Letter; *see also* BlackRock Letter. We do

threshold at $150 million to match the new private fund adviser exemption under section 203(m) of the Advisers Act.[55] From the perspective of systemic risk monitoring, it does not appear at this time that the value of gathering this information from registered advisers with less than $150 million in private fund assets under management justifies the burden to these advisers.

Most private fund advisers that are required to file Form PF will only need to complete section 1 of the Form. This section requires advisers to provide certain basic information regarding any private funds they advise in addition to information about their private fund assets under management and their funds' performance and use of leverage. We describe the information to be collected under section 1 of Form PF in further detail in section II.C.1 of this Release.

As discussed below, however, certain larger private fund advisers must complete additional sections of Form PF, which require more detailed information.[56] Specifically,

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not believe that a threshold based on fund size would be appropriate because the aggregate amount of assets in smaller funds that an adviser controls may contribute significantly to the adviser's total ability to affect financial markets and the $150 million minimum reporting threshold that we are adopting, based on the adviser's private fund assets under management, will adequately differentiate between advisers with only smaller funds and those with significant fund assets.

55 *See* IAA Letter.

56 *See* Instruction 3 to Form PF. With this scaled approach, the reporting requirements we are adopting reflect the Dodd-Frank Act directive that, in formulating systemic risk reporting and recordkeeping for investment advisers to mid-sized private funds, the SEC take into account the size, governance, and investment strategy of such funds to determine whether they pose systemic risk. *See* section 203(n) of the Advisers Act. The Dodd-Frank Act also provides that the SEC may establish different reporting requirements for different classes of fund advisers, based on the type or size of private fund being advised. *See* section 204(b) of the Advisers Act.

three types of "Large Private Fund Advisers" would be required to complete certain additional sections of Form PF:

- Any 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;[57]
- Any adviser managing a liquidity fund and having 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;[58] and
- Any adviser having at least $2 billion in regulatory assets under management attributable to private equity funds as of the last day of the adviser's most recently completed fiscal year.[59]

These large advisers must complete additional sections of Form PF, with large hedge fund advisers completing section 2 and large liquidity fund and private equity fund advisers completing sections 3 and 4, respectively.[60] The information each of these

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57 *See* Instruction 3 to Form PF. To determine whether an adviser must file a quarterly report at the end of the second quarter, it must look to its hedge fund assets under management as of the end of each month in the first quarter. *See infra* text accompanying note 112. We have modified the amount of this threshold from the proposal. For a discussion of this modification and the reasons for establishing the threshold at this amount, see below in section II.A.4.a of this Release (including notes 90-92 and accompanying text).

58 *See supra* note 57. For a discussion of the reasons for establishing the threshold at this amount, see below in section II.A.4.a of this Release.

59 *See* Instruction 3 to Form PF. For a discussion of the reasons for establishing the threshold at this amount, see below in section II.A.4.a of this Release.

60 As adopted, Form PF requires advisers to determine whether they meet the large adviser thresholds less frequently than was proposed (quarterly rather than daily for hedge fund

sections requires is tailored to the type of fund, focusing on relevant areas of financial activity that have the potential to raise systemic concerns. We discuss these areas of financial activity as they relate to hedge funds, liquidity funds and private equity funds in greater detail in the Proposing Release and below.[61]

1. "Hedge Fund" Definition

Registered advisers managing hedge funds must submit information on Form PF regarding the financing and activities of these funds in section 1 of the Form, and large hedge fund advisers are required to provide additional information in section 2 of the Form.[62] Form PF defines "hedge fund" generally to include any private fund having any one of three common characteristics of a hedge fund: (a) a performance fee that takes into account market value (instead of only realized gains); (b) high leverage; or (c) short

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and liquidity fund advisers and annually rather than quarterly for private equity advisers). We discuss this change in section II.A.4 of this Release.

61 *See* sections II.A.1, II.A.2 and II.A.3 of the Proposing Release, *supra* note 12, and sections II.C.2, II.C.3 and II.C.4 of this Release.

62 Several commenters debated whether the hedge fund industry generally, or any hedge fund in particular, could pose systemic risk. *See, e.g.*, AFL-CIO Letter and CII Letter, identifying hedge fund activities that could have systemic consequences; and AIMA General Letter and MFA Letter, arguing that no hedge fund operating today is likely to be systemically significant. Even among skeptical commenters, however, there was recognition that "there is no concrete data to draw conclusions either way, and that the exercise [of reporting] will be useful to allow the FSOC to make evidence-based conclusions." AIMA General Letter; *see also* MFA Letter. As discussed in the Proposing Release, we believe that Congress expected hedge fund advisers would be required to report under Title IV of the Dodd-Frank Act and that information regarding certain activities of hedge funds may be important to FSOC's monitoring of systemic risk. *See* Proposing Release, *supra* note 11, at nn. 54-61 and accompanying text.

selling.[63] 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.

A number of commenters addressed the "hedge fund" definition. Some of these suggested that we eliminate the distinctions among fund types and instead require all advisers to complete the entire Form so that advisers could not use the definitions to avoid reporting requirements.[64] Others, however, urged us to narrow the definition so that fewer funds would be classified as hedge funds.[65] Form PF generally requires more information regarding hedge funds than other types of funds, and in most cases, an adviser must conclude that a fund is not a hedge fund in order to classify it as one of the six other types of private fund defined in Form PF.[66] As a result, narrowing the "hedge fund" definition in Form PF could have a significant effect on reporting. Commenters persuaded us, however, that certain revisions to the proposed definition would result in a more accurate grouping of funds, thereby improving the quality of the data collected and, at the same time, reducing the reporting burdens on some advisers.[67]

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63 *See* Glossary of Terms to Form PF. We are defining the term "hedge fund" in Form PF solely for purposes of determining what information an adviser is required to report on the Form. This definition does not apply with respect to any other form or regulation of either Commission unless otherwise specified. The SEC has recently adopted this same definition in amendments to Form ADV. *See* Implementing Adopting Release, *supra* note 11, at nn. 248-255 and accompanying text. The CFTC has not adopted any definition of "hedge fund" beyond that adopted solely for purposes of Form PF.

64 *See, e.g.*, AFL-CIO Letter.

65 *See, e.g.*, ABA Committees Letter; AIMA General Letter; IAA Letter; PEGCC Letter; SIFMA Letter; comment letter of TCW Group, Inc. (Apr. 12, 2011) ("TCW Letter").

66 *See* Glossary of Terms to Form PF. Altogether, the seven types of private fund defined in Form PF are: (1) hedge fund; (2) liquidity fund; (3) private equity fund; (4) real estate fund; (5) securitized asset fund; (6) venture capital fund; and (7) other private fund.

67 The "hedge fund" definition, as well as the six other private fund definitions used in Form PF, are also included in the SEC's recent revisions to Form ADV. *See*

First, we have expressly excluded from the "hedge fund" definition in Form PF vehicles established for the purpose of issuing asset backed securities ("securitized asset funds").[68] One commenter noted that these funds could have been categorized as hedge funds under our proposal, which was not the intended result.[69] Although the issuance of asset backed securities may have systemic risk implications, the questions on Form PF regarding hedge funds would not yield relevant data regarding securitized asset funds. As a result, including responses regarding securitized asset funds in the hedge fund data could distort the information FSOC obtains from questions directed at hedge funds.

Second, we have modified clause (a) of the "hedge fund" definition in Form PF, which classifies a fund as a hedge fund if it uses performance fees or allocations that are calculated by taking into account unrealized gains. One commenter pointed out that even

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Implementing Adopting Release, *supra* note 11, at section II.C.1. Although the SEC received no comments on these same definitions in the context of that rulemaking, the SEC believes that having consistent definitions in the two forms is important. As a result, the SEC considered in the context of that rulemaking the comments received on these definitions in Form PF and determined, when adopting revisions to Form ADV, to make several changes in that form. The changes we are making to these definitions as used in Form PF conform the two sets of definitions so that both forms use identical terms (with the exception that, for purposes of Form PF, all commodity pools about which an adviser is reporting are treated as hedge funds, while in Form ADV, only commodity pools that are private funds are treated as hedge funds). *See* Implementing Adopting Release, *supra* note 11, at nn 248-255. The CFTC has not adopted any definition of "hedge fund" beyond that adopted solely for purposes of Form PF.

68 Specifically, the "hedge fund" definition in Form PF now refers to any private fund having one of the listed characteristics and excludes securitized asset funds. Under the proposal, a fund that satisfied the "hedge fund" definition would have been categorized as a hedge fund even if it otherwise would have satisfied the "securitized asset fund" definition. As adopted, Form PF defines "securitized asset fund" as any private fund "whose primary purpose is to issue asset backed securities and whose investors are primarily debt-holders." We have also modified this definition from the proposal so that it is no longer defined by reference to the "hedge fund" definition. *See* Glossary of Terms to Form PF.

69 *See* TCW Letter.

funds that do not allow for the payment of such fees or allocations, such as private equity funds, may be required to accrue or allocate these amounts in their financial statements to comply with applicable accounting principles.[70] It was not intended for funds that accrue or allocate these fees or allocations solely for financial reporting purposes to be classified as hedge funds, so we have clarified that clause (a) relates only to fees or allocations that may be *paid* to an investment adviser (or its related persons).[71]

Third, we have addressed another commenter's concern that clause (a) could inadvertently capture certain private equity funds because, although these funds typically calculate currently payable performance fees and allocations based on realized amounts, they will sometimes reduce these fees and allocations by taking into account "unrealized losses net of unrealized gains in the portfolio."[72] Funds should not be classified as hedge funds for purposes of Form PF based solely on this practice, and we have clarified that clause (a) would not include performance fees or allocations the calculation of which

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70 *See* TCW Letter.

71 Some commenters objected to clause (a) of the "hedge fund" definition more generally, arguing that it is too broad because some traditional/long only funds use performance fees or allocations calculated by taking into account unrealized gains. *See, e.g.*, AIMA General Letter; TCW Letter. However, based on our staffs' discussions with staff representing FSOC's members, we believe that funds using these types of fees are often active in markets that FSOC may desire to monitor for concentration risks. In addition, Form PF is intended to provide FSOC with a broad picture of the private fund industry so that it has context against which to assess systemic risk. An important part of this is gathering information about funds with similar characteristics, such as performance fees based on unrealized gains, so that industry-wide comparisons can be made. The inclusion of any particular fund in a reporting group, whether as a result of the private fund definitions or the reporting thresholds, does not represent a conclusion that the fund engages in activities that pose systemic risk.

72 *See* PEGCC Letter.

may take into account unrealized gains solely for the purpose of reducing such fees or allocations to reflect net unrealized losses.

Finally, several commenters asserted that clause (c) of the "hedge fund" definition, which looks to whether a fund may engage in short selling, should include an exception for a *de minimis* amount of short selling or exclude short selling intended to hedge the fund's exposures.[73] However, short selling appears to be, for purposes of Form PF, a potentially important distinguishing feature of hedge funds, many of which may, as the name suggests, use short selling to hedge or manage risk of various types. On the other hand, we also understand that many funds pursuing traditional investment strategies use short positions to hedge foreign exchange risk and to manage the duration of interest rate exposure, and we are persuaded that including funds within the definition of "hedge fund" in Form PF solely because they use these particular techniques would dilute the meaningfulness of the category. Therefore, we have modified clause (c) to provide an exception for short selling that hedges currency exposure or manages duration.[74]

Commenters arguing that, instead of a definition, the Commissions should take an approach similar to that used in the FSA Survey, which outlined common hedge fund characteristics and allowed an adviser "to make its own good faith judgment as to

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73 *See* IAA Letter; PEGCC Letter; SIFMA Letter; TCW Letter.

74 We have also made a change to clause (c) to clarify that this clause includes traditional short sales and any transaction resulting in a short exposure to a security or other asset (such as using a derivative instrument to take a short position). The purpose of this definition is to categorize funds that engage in certain types of market activity, and therefore, whether the definition applies should not depend on the form in which the fund engages in that activity.

whether a particular fund is a hedge fund," were not persuasive.[75] Such an approach could effectively defer to the adviser the determination of whether to report on Form PF information about hedge funds – an approach that might be appropriate for a voluntary survey, like the FSA's, but one that would significantly compromise the value of data collected for FSOC and thus would fail to achieve the purpose of this rulemaking.

Two other commenters suggested instead that we eliminate all of the private fund definitions and require that every private fund adviser complete the entire Form.[76] These commenters were concerned that any distinction among funds tied to the amount or type of information required would encourage advisers to change strategies in order to avoid reporting. Although we are sensitive to these concerns, we believe that distinguishing fund types is important for two reasons. First, by distinguishing among types of funds, we are able to limit the information collection burdens on advisers to funds for which the information is most relevant.[77] Second, separating reported data by fund strategy allows extraneous information to be excluded, which we believe will improve its utility to FSOC and the Commissions.

Several commenters also expressed concern that clauses (b) and (c) of the "hedge fund" definition in Form PF are too broad because many funds have the capacity to

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75 ABA Committees Letter. *See also* AIMA General Letter; IAA Letter; Seward Letter.

76 *See* AFL-CIO Letter; AFR Letter.

77 For instance, one commenter, in agreeing that Form PF appropriately differentiates "between the reporting requirements for hedge funds and private equity funds," pointed out that section 2 of the Form, which would be completed by large hedge fund advisers, contains many questions that "are not relevant to private equity funds." This commenter also explained that requiring response to "questions that are not directly related to" the operations of private equity advisers would impose burdens on both FSOC and the advisers. *See* comment letter of Lone Star U.S. Acquisitions (Apr. 12, 2011) ("Lone Star Letter").

borrow or incur derivative exposures in excess of the specified amounts or to engage in short selling but do not in fact engage, or intend to engage, in these practices.[78] These commenters generally argued that clauses (b) and (c) should focus on actual or contemplated use of these practices rather than potential use. Changes to the "hedge fund" definition in response to these comments have not been made because clauses (b) and (c) properly focus on a fund's ability to engage in these practices. Even a fund for which leverage or short selling is an important part of its strategy may not engage in that practice during every reporting period. Thus, the suggested approach could result in incomplete data sets for hedge funds, a class of funds that may be systemically significant. However, 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 (other than, in the case of clause (c), short selling for the purpose of hedging currency exposure or managing duration) and a reasonable investor would understand, based on the fund's offering documents, that the fund will not engage in these practices.

Finally, some commenters recommended that a fund should not be classified as a "hedge fund" for purposes of Form PF unless it satisfies at least two of the prongs of the "hedge fund" definition (rather than any one prong).[79] The definition is designed to identify funds that are an appropriate subject for the higher level of reporting to which

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78 *See, e.g.*, AIMA General Letter; IAA Letter; PEGCC Letter; SIFMA Letter; TCW Letter.

79 *See, e.g.*, Lone Star Letter; PEGCC Letter; TCW Letter.

hedge funds will be subject under Form PF, and, based on our staffs' consultations with staff representing FSOC's members, we believe that any one of the identified characteristics is sufficient to appropriately distinguish a fund for this purpose. We have not, therefore, made the change these commenters suggested. The changes to the "hedge fund" definition discussed above are intended to more accurately group private funds for purposes of Form PF and, thereby, improve the quality of information reported.

2. "Liquidity Fund" Definition

Registered advisers managing liquidity funds must submit information on Form PF regarding the financing and activities of these funds in section 1 of the Form, and large liquidity fund advisers are required to provide additional information in section 3 of the Form.[80] For purposes of Form PF, a "liquidity fund" is any 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 unit or minimize principal volatility for investors.[81] Commenters did not address the "liquidity fund" definition, which the SEC is adopting as proposed.

3. "Private Equity Fund" Definition

Registered advisers managing private equity funds must submit information on Form PF regarding the financing and activities of these funds in section 1 of the Form,

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80 Form PF is a joint form between the SEC and the CFTC only with respect to sections 1 and 2 of the Form. Section 3 of the Form, which requires more specific reporting regarding liquidity funds, is only required by the SEC.

81 *See* Glossary of Terms to Form PF. As discussed in the Proposing Release, liquidity funds can resemble registered money market funds, certain features of which may make them susceptible to runs and thus create the potential for systemic risk. *See* Proposing Release, *supra* note 12, at section II.A.2.

and large private equity advisers are required to provide additional information in section 4 of the Form.[82] Consistent with the proposal, Form PF defines "private equity fund" as 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.[83] Two commenters advocated for a definition of "private equity fund" that would not depend on whether a fund is a hedge fund.[84] This approach could, however, create gaps between the definitions and encourage advisers to structure around the reporting requirements.[85] The changes we have made to the "hedge fund" definition substantially address the concerns of these commenters.[86] Therefore, we

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82 Form PF is a joint form between the SEC and the CFTC only with respect to sections 1 and 2 of the Form. Section 4 of the Form, which requires more specific reporting regarding private equity funds, is only required by the SEC.

83 *See* Glossary of Terms to Form PF. The definitions of "real estate fund" and "venture capital fund" are being adopted as proposed, and changes to the definition of "securitized asset fund" are discussed above. *See supra* note 69. These definitions are primarily intended to exclude these types of funds from our definition of "private equity fund" to improve the quality of data reported on Form PF relating to private equity funds.

84 *See* PEGCC Letter (proposing an alternative that largely inverts the proposed "hedge fund" definition but would allow for short selling and soften other distinctions); SIFMA Letter (suggesting an alternative that would define a "private equity fund" as a private fund having "a large number of sophisticated, third-party institutional and high net worth investors" and satisfying ten additional criteria, including that "the fund and its investment activities are not subject to regulatory restrictions or limitations.").

85 Some commenters were concerned that creating any distinctions among funds would encourage advisers to change strategies in order to avoid reporting. *See supra* note 76 and accompanying text. The SEC believes, based on its staff's consultations with staff representing FSOC's members, that this risk is best addressed by tightly integrating the definitions.

86 *See supra* notes 64-79 and accompanying text for a discussion of comments on the "hedge fund" definition and the changes we are making from the proposal. Some of these comments reflected concern that the breadth of the "hedge fund" definition would cause it to capture some private equity funds. Commenters arguing for an independent "private equity fund" definition expressed similar concerns. As discussed above, certain

believe that the proposed approach to defining "private equity fund" continues to be appropriate for the purposes of Form PF.

4. Large Private Fund Adviser Thresholds

a. Amounts

As noted above, we are adopting a threshold of $1.5 billion in hedge fund assets under management for large hedge fund adviser reporting, $1 billion in combined liquidity fund and registered money market fund assets under management for large liquidity fund adviser reporting, and $2 billion in private equity fund assets under management for large private equity fund adviser reporting.[87] These thresholds are designed so that the group of Large Private Fund Advisers filing Form PF will be relatively small in number but represent a substantial portion of the assets of their respective industries. For example, we estimate that approximately 230 U.S.-based advisers each managing at least $1.5 billion in hedge fund assets represent over 80 percent of the U.S. hedge fund industry based on assets under management.[88] Similarly,

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of the changes we are making to the "hedge fund" definition are designed to address these concerns.

87 As proposed, we are requiring that an adviser determine whether it meets a threshold and qualifies as a large hedge fund adviser, large liquidity fund adviser or large private equity adviser based solely on the assets under management attributable to the particular types of fund. Two commenters suggested that we instead require advisers to aggregate all of their assets under management, regardless of strategy, for purposes of the thresholds. *See* AFL-CIO Letter; AFR Letter. These commenters cautioned that our approach could allow advisers with substantial private fund assets under management to nevertheless avoid classification as a Large Private Fund Advisers. We are sensitive to these commenters' concerns, but we continue to believe that the hedge fund, liquidity fund and private equity fund business models are sufficiently distinct that for FSOC's purposes they are most appropriately analyzed on a separate basis.

88 *See Billion Dollar Club*, HEDGEFUND INTELLIGENCE ("HFI") (Oct. 3, 2011). We estimate that, in addition to the 230 U.S.-based hedge fund advisers that will exceed the threshold, approximately 23 non-U.S. private fund advisers will also be classified as large

SEC staff estimates that the approximately 155 U.S.-based advisers each managing over $2 billion in private equity fund assets represent approximately 75 percent of the U.S. private equity fund industry based on committed capital.[89]

The threshold we are adopting for large hedge fund advisers reflects an increase from the $1 billion threshold that we proposed. We do not expect, however, that this increase will substantially change the group of advisers that were estimated in the proposal would be classified as large hedge fund advisers. Rather, the change is intended simply to adjust for a difference in how assets under management are measured in Form PF compared to how they are measured in the commercial databases that we consulted in

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hedge fund advisers, for a total of approximately 250 large hedge fund advisers. We have based this estimate of non-U.S. advisers on IARD data as of October 1, 2011, showing that, among currently registered private fund advisers, fewer than 10% are non-U.S. advisers. (We are not aware of any reason that recent changes in the exemptions available under the Advisers Act would affect the relative representation of U.S. and non-U.S. advisers.) One commenter suggested that estimates based on HFI data should be grossed up because the database is under-inclusive. *See* comment letter of the Alternative Investment Management Association (Jul. 26, 2011) ("AIMA AUM Letter"). Although we acknowledge that this database is likely somewhat under-inclusive, we believe that the amount of assets under management not represented in the database is relatively small because the aggregate amount of assets reported to the database is consistent with other data sources estimating the total size of the hedge fund industry. In addition, we believe the uncounted assets are likely skewed toward the smaller advisers in the industry because the identity and size of the industry's largest advisers are relatively consistent across sources. As a result, although this database may under-represent the total amount of hedge fund industry assets under management, the count of large hedge fund advisers is likely to be relatively accurate. The changes to the "hedge fund" definition discussed above will likely result in fewer funds being classified as hedge funds than under the proposed definition. However, these changes are intended to more accurately group private funds for purposes of Form PF and should more closely align the definition to the estimates discussed above.

89 Preqin. The Preqin data relating to private equity fund committed capital is available in File No. S7-05-11. We estimate that, in addition to the 155 U.S.-based private equity advisers that will exceed the threshold, approximately 16 non-U.S. private fund advisers will also be classified as large private equity advisers, for an approximate total of 170 large private equity advisers. *See supra* note 88 for a discussion of the basis for this estimate.

proposing the $1 billion threshold amount. Form PF uses the definition of "regulatory assets under management" that the SEC recently adopted in connection with amendments to its Form ADV. This definition measures assets under management *gross* of outstanding indebtedness and other accrued but unpaid liabilities. One commenter pointed out, however, that the assets under management that advisers report to the currently available third-party databases are generally calculated on a *net* basis.[90] In other words, without adjustment, our proposed threshold of $1 billion in gross assets would have captured advisers with less than $1 billion in net assets, expanding the group of advisers classified as large hedge fund advisers beyond what we intended.[91] We believe this revised threshold strikes an appropriate balance between obtaining

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90 *See* AIMA AUM Letter.

91 We are not aware of any existing source with data regarding the gross assets under management of U.S. hedge fund managers. Therefore, based on our staffs' consultations with staff representing FSOC's members, we have established this threshold by multiplying the proposed threshold by an industry average leverage ratio of 1.5 times net assets. The commenter suggested that industry leverage ranges between 1.5 and 3 times net assets but noted that leverage ratios over the preceding 12 months had dropped to 1.1 times investment capital. *See* AIMA AUM Letter; *see also* MFA Letter (citing leverage ratios from 3.0 to as low as 1.16); Andrew Ang, *et al.*, *Hedge Fund Leverage*, NATIONAL BUREAU OF ECONOMIC RESEARCH (Feb. 2011). We have used a leverage ratio at the lower end of this range because, without data regarding the industry's gross assets, it cannot confidently be estimated that a higher threshold would capture a portion of the industry sufficient to allow FSOC to effectively perform systemic risk assessments. Also, although the definition of "regulatory assets under management" is measured gross of certain liabilities, it does not capture all forms of leverage that may be included in the sources cited in the AIMA AUM Letter, such as off-balance sheet leverage. As a result, the leverage implied by "regulatory assets under management" may be lower than the leverage estimated based on these sources. The AIMA AUM Letter also suggested that the average leverage ratio used should be asset-weighted because advisers with over $1 billion in net assets under management tend to use greater amounts of leverage. However, these larger advisers would exceed the threshold even if measured on a net basis. The adjustment to the threshold to account for leverage is most relevant for the middle group of advisers, not the large advisers, and the leverage ratio we have used is consistent with the leverage ratio this commenter estimates for advisers with $200 million to $1 billion in net assets under management.

information regarding a significant portion of the hedge fund industry while minimizing the burden imposed on smaller advisers.[92]

An adviser managing liquidity funds must combine liquidity fund and registered money market fund assets for purposes of determining whether it meets the threshold for more extensive reporting regarding its liquidity funds. Liquidity funds and registered money market funds often pursue similar strategies, invest in the same securities and present similar risks. An adviser is, however, only required to report information about unregistered liquidity funds on Form PF. This information will supplement data the SEC collects about registered money market funds on its Form N-MFP and provide FSOC a more complete picture of large liquidity pools and their management. The SEC expects this approach to the reporting threshold to capture approximately 80 of the most significant managers of liquidity funds.[93] Commenters supported this approach, which we are adopting as proposed.[94]

Based on our staffs' consultations with staff representing FSOC's members, we believe that requiring basic information from all registered advisers over the minimum reporting threshold but more extensive and detailed information only from advisers meeting the higher thresholds is important to enabling FSOC to obtain a broad picture of

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92 Similar adjustments to the thresholds applicable to liquidity fund advisers and private equity fund advisers have not been made because we understand these strategies typically involve little leverage at the fund level. *See infra* note 306 and accompanying text.

93 *See also* Proposing Release, *supra* note 12, at n. 89. The estimate of the number of large liquidity fund advisers is based on the number of advisers with at least $1 billion in registered money market fund assets under management, as reported on Form N-MFP as of October 1, 2011.

94 *See* AFL-CIO Letter; AFR Letter.

the private fund industry. We understand that obtaining this broad picture will help FSOC to contextualize its analysis and assess whether systemic risk may exist across the private fund industry and to identify areas where OFR may want to obtain additional information. At the same time, requiring that only these Large Private Fund Advisers complete additional reporting requirements under Form PF will provide systemic risk information for a substantial majority of private fund assets while minimizing burdens on smaller private fund advisers that are less likely to pose systemic risk concerns.

Although thresholds set at a higher amount could still yield information regarding much or a majority of the private fund industry's assets under management, such thresholds would potentially impede FSOC's ability to obtain a representative picture of the private fund industry. The activities of private fund advisers may differ significantly depending on size because, for instance, some strategies may be practical only at certain scales.[95] As a result, obtaining information regarding, for instance, 50 percent or 60 percent of the industry's assets under management may not be sufficient to confidently draw conclusions regarding the remaining portion of the industry. However, because relatively few advisers manage most of the industry's assets under management, a substantial reduction in the potential burdens of reporting can be achieved without sacrificing the ability to obtain a more representative picture. For example, setting the

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[95] For example, one commenter cited evidence suggesting that the use of leverage varies significantly with fund size, though they did not state whether this variation continues among advisers with over $1 billion in net assets under management. *See* AIMA AUM Letter. *See also* Ibbotson, Roger G., Peng Chen, and Kevin X. Zhu, 2011, *The ABCs of Hedge Funds: Alphas, Betas, and Costs*, FINANCIAL ANALYSTS JOURNAL 67 (1) ("Ibbotson, et al.") at 17-18 (discussing possible explanations for observed differences in returns for larger and smaller hedge funds).

threshold to cover, for instance, 80 percent of industry assets under management rather than 100 percent would relieve thousands of advisers from more detailed reporting while still obtaining a reasonably representative picture.[96] There are, however, limits to the range within which this tradeoff can be effectively made. For example, setting the thresholds to cover, for instance, 60 percent of industry assets under management rather than 80 percent would relieve a relatively small segment of advisers from more detailed reporting but might not result in a picture broad enough to be representative. Accordingly, the thresholds have been established to balance FSOC's need for a broad, representative set of data regarding the private fund industry with the desire to limit the potential burdens of private fund systemic risk reporting.

Commenters expressed support for a tiered reporting system based on size.[97] However, most commenters thought the proposed threshold of $1 billion was either too high or too low.[98] Commenters arguing for a lower threshold expressed concern that, at $1 billion, regulators would receive insufficient information to monitor certain types of market behavior with potentially systemic consequences.[99] In contrast, a number of

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96 In the PRA analysis below, the SEC estimates that the large adviser thresholds will result in approximately 500 advisers reporting additional information in section 2, 3 or 4 of Form PF while approximately 3,070 advisers will report information only in section 1 and another 700 will not report on Form PF at all because of the minimum reporting threshold. *See infra* section IV.A of this Release.

97 *See*, *e.g.*, comment letter of Coalition of Private Investment Companies (Mar. 31, 2011) ("CPIC Letter") and MFA Letter.

98 Compare AFL-CIO Letter and AFR Letter (supporting a lower threshold) to AIMA General Letter; IAA Letter; MFA Letter; PEGCC Letter; SIFMA Letter (supporting a higher threshold). *See also* comment letter of George Merkl (Feb. 22, 2011) ("Merkl February Letter") (supporting the proposed thresholds).

99 *See* AFL-CIO Letter (arguing that the proposal would not allow regulators to monitor "herding" behavior, which it defines as the tendency for market participants to trade

commenters argued that even an adviser with $1 billion in assets under management could not pose systemic risk.[100] Several of these commenters supported an increase to $5 billion, which they argued would still capture over half the hedge fund industry while ensuring that advisers have sufficient operational capabilities to complete the Form.[101]

We have carefully considered these comments in light of the information we understand FSOC desires and its intended use by FSOC. Based on this, the SEC has determined to adopt the proposed threshold for large liquidity fund advisers and to increase the threshold for large private equity fund advisers to $2 billion. We are adopting the threshold for large hedge fund advisers with the corrective change discussed

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together on one side of the market; also suggesting that, at a minimum, advisers with between $150 million and $1 billion in assets under management "should be required to complete all applicable sections of Form PF on a semi-annual basis."); AFR Letter.

100 *See, e.g.*, AIMA General Letter (also questioning whether the SEC and FSOC have the capacity to analyze the data from all the advisers above the proposed threshold); IAA Letter; MFA Letter; comment letter of Olympus Partners (Apr. 1, 2011) ("Olympus Letter"); PEGCC Letter (preferring that there be no large adviser category for private equity fund advisers because, in their view, these advisers pose little systemic risk); Seward Letter; SIFMA Letter; comment letter of the United States Chamber of Commerce, Center for Capital Markets Competitiveness (Apr. 12, 2011) ("USCC Letter").

101 *See, e.g.*, AIMA General Letter (asserting that a $5 billion threshold "still captures around 50-60% of the US hedge fund industry assets or just over 75 large hedge fund managers."); MFA Letter ("Based on estimates, 77 hedge fund managers representing approximately 50-60% of hedge fund industry assets would exceed this [$5 billion] threshold."); Seward Letter; USCC Letter (citing figures similar to those provided in the AIMA General Letter and the MFA Letter in support of a $5 billion threshold). Other commenters asserted that the thresholds should take into account measures of leverage or derivatives exposures rather than just assets under management. *See, e.g.*, ABA Committees Letter; AIMA General Letter. As discussed above, measuring these thresholds using "regulatory assets under management," as defined in Form ADV, implies adjustment for some forms of leverage. Two commenters suggested that, instead of assets under management, the adviser's proprietary assets are the most appropriate measure of assets at risk. *See* PEGCC Letter; USCC Letter. However, private fund advisers exercise significant discretion over the assets they manage, which makes assets under management a more accurate measure of an adviser's ability to affect the U.S. financial system.

above. Although we understand commenters' concerns that the proposed thresholds are too high and will not permit regulators to detect certain group behaviors among smaller private fund advisers, we believe at this time that the amount of additional information that would be required for this purpose would impose a significant burden on these smaller advisers and not significantly expand FSOC's ability to understand the industry.

On the other hand, in light of the information we understand FSOC desires and its intended use by FSOC, we are also not persuaded that a larger increase in the thresholds would be appropriate. Commenters supporting an increase may be correct that an adviser just exceeding these thresholds could not be large enough to pose systemic risk. However, the thresholds are not intended to establish a cutoff separating the risky from the safe but rather to provide FSOC with sufficient context for the assessment of systemic risk while minimizing the burden imposed on smaller advisers.[102] We understand based on our staffs' consultation with staff representing FSOC's members that, in order to assess potential systemic risk posed by the activities of certain funds, FSOC would benefit from access to data about funds that, on an individual basis, may not be a source of systemic risk. As discussed above, the increase that some commenters supported would result in coverage of a substantially smaller part of the industry, potentially impeding FSOC's ability to obtain a broad picture of the private fund industry.[103]

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102 *See supra* text accompanying notes 94-96. As noted above, the FSOC Second Notice highlights that even establishing guidelines for evaluating private fund advisers may require the context that Form PF will provide. *See supra* note 21.

103 In particular, the activities of private fund advisers may differ significantly depending on size and that the portion of industry assets represented by advisers with over $5 billion in private fund assets under management may look substantially different from the portion

The SEC is, however, persuaded that an increase in the threshold for large private equity advisers that is smaller than some commenters advocated can be made without sacrificing the ability to obtain a broad picture of the private equity industry. SEC staff estimates that an increase in this threshold to $2 billion from the proposed $1 billion will reduce the portion of U.S. private equity industry assets covered by the more detailed reporting in section 4 of the Form from approximately 85 percent to approximately 75 percent.[104] At the same time, it reduces the number of U.S.-based advisers SEC staff estimates will be categorized as large private equity advisers from approximately 270 to approximately 155.[105] This will significantly mitigate the number of advisers subject to the more detailed reporting while still covering a substantial majority of industry assets. As a result of this change, section 4 of Form PF will cover a smaller portion of U.S. private equity industry assets than section 2 covers of U.S. hedge fund industry assets. However, the SEC believes this result is appropriate because private equity funds tend to pursue a narrower range of strategies than hedge funds, reducing concerns regarding the level of representativeness.

b. Frequency of Testing

The proposal would have required hedge fund and liquidity fund advisers to measure whether they had crossed these thresholds on a daily basis and private equity advisers to measure them on a quarterly basis. The proposed approach was based on our

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of industry assets represented by advisers with between, for instance, $1 billion and $5 billion.

104 *See supra* note 89.

105 *See supra* note 89.

understanding that, as a matter of ordinary business practice, advisers are aware of hedge fund and liquidity fund assets under management on a daily basis, but are likely to be aware of private equity fund assets under management only on a quarterly basis.

However, several commenters argued that advisers would have difficulty monitoring on a daily basis the value of private funds holding complex or illiquid investments.[106] One commenter also noted that, in any given quarter, an adviser could experience significant spikes in the value of its assets under management.[107] These commenters suggested a variety of alternatives, such as testing at the end of the prior reporting period,[108] using an average over the period (possibly based on values at the end of each month in the quarter),[109] or testing at the end of each month.[110] We are persuaded that requiring daily testing of complex or illiquid investments could impose a substantial burden on some advisers, and we have, accordingly, modified the Form so that advisers need only test whether their hedge fund or liquidity fund assets meet the relevant threshold as of the end of each month.[111] In addition, as some commenters suggested, the test will look back one quarter so that these advisers know at the start of each reporting period whether they will be required to complete the more detailed reporting required of large hedge fund advisers and large liquidity fund advisers.[112] We did not adopt an

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106 *See, e.g.*, ABA Committees Letter; BlackRock Letter; MFA Letter; Seward Letter.

107 *See* ABA Committees Letter.

108 *See* BlackRock Letter; MFA Letter.

109 *See* ABA Committees Letter; AIMA General Letter; IAA Letter.

110 *See* Seward Letter.

111 *See* Instruction 3 to Form PF.

112 *Id. See also supra* note 108.

approach using an average because it would add unnecessary complexity and potentially allow an adviser whose assets under management have grown significantly during a quarter to delay more detailed reporting for an additional quarter.

Commenters also objected to the proposed quarterly testing with respect to private equity advisers, suggesting that even such infrequent testing may be difficult for some advisers.[113] As we discuss in further detail below, large private equity fund advisers will be required to report information regarding their private equity funds only on an annual (rather than quarterly) basis, with the result that quarterly testing of the threshold is unnecessary.[114] Accordingly, advisers need only test whether their private equity fund assets meet the relevant threshold at the end of each fiscal year.[115]

5. Aggregation of Assets under Management

For purposes of determining whether an adviser meets the $150 million minimum reporting threshold or is a Large Private Fund Adviser for purposes of Form PF, the adviser must aggregate together:

- assets of managed accounts 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")

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113 *See* Merkl February Letter (noting that some private equity funds do not provide first and third quarter financial statements to investors); PEGCC Letter (suggesting annual testing and asserting that the less volatile nature of private equity investments would not justify the cost of quarterly valuation).

114 *See* section II.B of this Release.

115 *See* Instruction 3 to Form PF.

unless the value of those accounts exceeds the value of the private funds with which they are managed;[116] and

- assets of private funds advised by any of the adviser's "related persons" other than related persons that are separately operated.[117]

These aggregation requirements are designed to prevent an adviser from avoiding Form PF reporting requirements by re-structuring how it provides advice.

We have modified these aggregation requirements from the proposal. As adopted, an adviser may exclude parallel managed accounts if the value of those accounts is greater than the value of the private funds with which they are managed.[118] This change recognizes that, as some commenters noted, an adviser managing a relatively small amount of private fund assets could end up crossing a reporting threshold simply because it has a significant separate account business using a similar strategy.[119] We believe this approach is consistent with section 204(b) of the Advisers Act, the focus of

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116 *See* Instructions 1, 3, 5, and 6 to Form PF; and Glossary of Terms to Form PF. *See also* definitions of "dependent parallel management account," "hedge fund assets under management," "liquidity fund assets under management," and "private equity fund assets under management" in the Glossary of Terms to Form PF.

117 *See* Instructions 3 and 5 to Form PF. "Related person" is defined generally as: (1) all of the adviser's officers, partners, or directors (or any person performing similar functions); (2) all persons directly or indirectly controlling, controlled by, or under common control with the adviser; and (3) all of the adviser's employees (other than employees performing only clerical, administrative, support or similar functions). For purposes of Form PF, a related person is "separately operated" if the advisers is not required to complete section 7.A. of Schedule D to Form ADV with respect to that related person. *See* Glossary of Terms to Form PF and Glossary of Terms to Form ADV. In addition, an adviser may, but is not required to, file one consolidated Form PF for itself and its related persons. *See infra* section II.A.6 of this Release.

118 *See supra* note 116.

119 *See* IAA Letter; TCW Letter.

which is private fund reporting.[120] We remain concerned, however, that advisers focusing on private funds may increasingly structure investments as separate accounts to avoid Form PF reporting requirements, which could diminish the utility to FSOC of the information collected on Form PF.[121] Accordingly, an adviser must still include the value of parallel managed accounts in determining whether it meets a reporting threshold if the value of those accounts is less than the value of the private funds managed using substantially the same strategy.[122]

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120 An adviser managing primarily separate accounts would, of course, still be subject to the applicable Form PF reporting requirements if its private fund assets, taken alone, would cause it to exceed one or more reporting thresholds.

121 Commenters disagreed over whether such evasion was likely. One commenter supported the proposed aggregation rules, agreeing that they "will prevent [an adviser from splitting itself] into smaller components to avoid reporting requirements that are triggered by the amount of assets that are managed by an investment adviser." Merkl February Letter. Another commenter, however, was skeptical that advisers would re-structure to avoid reporting because clients typically determine the structure of their investments. *See* IAA Letter. Although clients may in many cases dictate the form of investment, we believe that advisers are not without influence in such structuring decisions and may prefer to avoid reporting on Form PF. (We note that advisers, as fiduciaries, may not subordinate clients' interests to their own such as by altering the structure of investments in a way that is not in the client's best interest in an attempt to remain under the reporting thresholds.)

122 *See supra* note 116. Some commenters also encouraged us to narrow the definition of "parallel managed account" so that fewer accounts or fewer types of accounts would be covered. *See, e.g.*, AIMA General Letter; IAA Letter (suggesting that we replace "substantially the same" with the "same"); comment letter of the Investment Company Institute (Apr. 12, 2011); TCW Letter (suggesting we exclude registered investment companies, undertakings for collective investment in transferable securities (UCITS) and SICAVs). We have, however, determined to adopt this definition as proposed because we believe that it appropriately reflects the total amount of assets that an adviser is managing using a particular strategy. In addition, the changes we are making with respect to how these account assets are treated for purposes of the reporting thresholds, as well as changes discussed below that allow advisers not to aggregate these account assets with their private funds for reporting purposes, substantially address the concerns of these commenters. *See infra* note 335 and accompanying text.

We have also modified these aggregation requirements from the proposal so that advisers may exclude the assets under management of related persons that are separately operated.[123] There was general support for the proposed aggregation of related persons.[124] However, commenters argued that "[r]equiring aggregation of funds managed by 'any related person' is not possible for many large institutions such as a large firm which operates under separate business units with independent asset management functions and decision making by affiliated entities."[125]

We are persuaded that advisers may have difficulty gathering the information necessary to aggregate the assets of related persons whose operations are genuinely independent of their own and that, with an appropriate standard of separateness, the risk of evasion is substantially mitigated. Having considered several existing SEC standards of separateness, we believe that the most appropriate for this purpose is the standard the SEC recently adopted in Item 7.A of Form ADV for determining whether an adviser must complete section 7.A of Schedule D to that form with respect to a related person.[126] Although the Item 7.A standard was adopted for a somewhat different regulatory

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123 *See supra* note 117. *See also* Proposing Release, *supra* note 12, for the proposed version of Instructions 3, 5 and 6 to Form PF.

124 *See*, *e.g.*, Merkl February Letter.

125 TCW Letter. *See also* IAA Letter.

126 One commenter suggested that we use the standard under section 13 of the Securities Exchange Act of 1934 ("Exchange Act") or look to whether the related persons "share information about investment decisions on a real time basis." TCW Letter. We are concerned that using the standard under sections 13(d) and 13(g) of the Exchange Act would impose additional burdens on advisers as compared to the Item 7.A standard because advisers will not necessarily have considered the former in the ordinary course of business, and we believe the alternative proposed by this commenter would make it too easy to conclude that a related person is separately operated.

purpose, we believe it suits this role as well. In addition, every adviser filing Form PF will have already considered this standard with respect to its related persons, which means that applying the standard in the context of Form PF will impose little or no incremental burden on advisers. Accordingly, for purposes of determining whether an adviser meets one or more of the reporting thresholds, the adviser need only aggregate its private fund assets with those of its related persons for which it is required to complete section 7.A of Schedule D to Form ADV.[127]

For purposes of both the reporting thresholds and responding to questions on Form PF, an adviser may exclude any assets invested in the equity of other private funds.[128] In addition, if any of the adviser's private funds invests substantially all of its assets in the equity of other private funds and, aside from those investments, holds only cash, cash equivalents and instruments intended to hedge currency risk, the adviser may complete only section 1b with respect to that fund and otherwise disregard that fund.[129]

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127 *See supra* note 117. The relevant instruction to Item 7.A of Form ADV reads as follows: "You do not need to complete Section 7.A. of Schedule D for any related person if: (1) you have no business dealings with the related person in connection with advisory services you provide to your clients; (2) you do not conduct shared operations with the related person; (3) you do not refer clients or business to the related person, and the related person does not refer prospective clients or business to you; (4) you do not share supervised persons or premises with the related person; and (5) you have no reason to believe that your relationship with the related person otherwise creates a conflict of interest with your clients."

128 *See* Instruction 7 to Form PF. The adviser must, however, treat these assets consistently for purposes of Form PF. For example, an adviser may not count these assets when determining whether the fund's borrowing may exceed half its net asset value and then disregard these assets for purposes of the reporting thresholds. Although this instruction allows an adviser to disregard these investments in other private funds, it would not allow an adviser to disregard any liabilities of the private fund, even if incurred in connection with an investment in other private funds.

129 *See* Instruction 7 to Form PF. Solely for purposes of this instruction, an adviser is also permitted to treat as a private fund any non-U.S. fund that would be a private fund had it

These instructions are intended to avoid duplicative reporting, which reduces the burden of reporting for advisers and improves the quality of the data reported.

Based on our staffs' consultation with staff representing FSOC's members, we have expanded from the proposal the scope of assets that may be disregarded under this instruction. The proposed instruction would have allowed advisers to disregard only fund of funds that invest exclusively in other private funds.[130] Commenters expressed concern that the proposed instruction would prove too narrow to accommodate many funds of funds, noting that these funds often hold cash or some amount of direct investments.[131] These commenters generally sought a broader exclusion for funds of funds, suggesting alternatives that would allow these funds to hold essentially unlimited dollar amounts of direct investments while not reporting on Form PF.[132] In light of the purpose for which

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used U.S. jurisdictional means in offering its securities. A non-U.S. fund that has never used U.S. jurisdictional means in the offering of the securities it issues would not be a private fund. *See infra* note 134; Exemptions Adopting Release, *supra* note 11, at n.294 and accompanying text.

130 *See* the Proposing Release, *supra* note 12, for the proposed version of Instruction 7 to Form PF. We have also added a new Instruction 8, which clarifies that, except as provided in Instruction 7, all investments in other funds should be included for all purposes under Form PF but that advisers are not required to "look through" the other funds to the underlying assets (unless the other fund's purpose is to act as a holding company for the private fund's investments).

131 *See, e.g.*, ABA Committees Letter; comment letter of Akina Limited (Feb. 25, 2011) ("Akina Letter"); MFA Letter; PEGCC Letter; comment letter of Sidley Austin, LLP (submitted to the CFTC) (Apr. 12, 2011) ("Sidley Letter"); SIFMA Letter.

132 *Id*. Some commenters also suggested that advisers should not report even the limited information required in section 1b with respect to funds of funds. *See, e.g.*, ABA Committees Letter; Sidley Letter; SIFMA Letter. However, as one commenter pointed out, these funds may be employing leverage at the fund of funds level, which would not be reported if these funds did not complete this section. *See* Merkl February Letter. In addition, information collected in section 1b will provide regulators with information regarding the extent of these funds' investments in other private funds, and certain of the information collected in this section may be important to our investor protection mission. *See infra* notes 133 and 197.

information is collected on Form PF, we are not convinced that an adviser should not have to report on a fund's direct investments simply because it primarily holds investments in other private funds. However, we are persuaded that our proposed exception for funds of funds was too narrow in that it did not allow for a *de minimis* amount of cash, cash equivalents and currency hedges. These limited non-private fund holdings appear unlikely, on their own, to raise systemic concerns. We are also persuaded that, even where a fund is not necessarily a "fund of funds" but holds investments in other private funds, reporting on those investments is unnecessary because information regarding the other private funds will, in most cases, be reported separately on Form PF, and we have modified the instructions accordingly.[133]

If an adviser's principal office and place of business is outside the United States, the adviser may exclude any private fund that, during the adviser's last fiscal year, was not a United States person, was not offered in the United States, and was not beneficially owned by any United States person.[134] This approach is designed to reduce the

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133 *See* Instruction 7 to Form PF. We have, however, added a new question 10 to Form PF, which requires the adviser to disclose the amount that each private fund has invested in other private funds. This will allow regulators to understand the extent to which these investments occur and are otherwise being disregarded on Form PF. *See infra* note 197.

134 *See* Instruction 1 to Form PF. This portion of Instruction 1 is only necessary for those funds that fall within the definition of "private fund." A non-U.S. fund that has never used U.S. jurisdictional means in the offering of the securities it issues would not be a private fund. *See* Exemptions Adopting Release, *supra* note 11, at n.294 and accompanying text. We have modified this instruction from the proposal to more closely follow the requirements of Regulation S; the instruction now looks to whether the offering was made "in the United States" rather than "to... any *United States person*." *See also* Glossary of Terms to Form PF. "United States person" is defined for purposes of Form PF by reference to the definition in rule 203(m)-1, which tracks the definition of a "U.S. person" under Regulation S but contains a special rule for discretionary accounts maintained for the benefit of United States persons. *See* Exemptions Adopting Release, *supra* note 11, at section II.B.4.

duplication of reporting requirements that foreign regulators may impose and to allow an adviser to report with respect to only those private funds that are more likely to implicate U.S. regulatory interests.

6. Reporting for Affiliated and Sub-advised Funds

An adviser may, but is not required to, report the private fund assets that it manages and the private fund assets that its related persons manage on a single Form PF.[135] This is intended to provide private fund advisers with reporting flexibility and convenience, allowing affiliated entities that share reporting and risk management systems to report jointly while also permitting affiliated entities that operate separately to report separately. Commenters did not address this aspect of the proposal, which we are adopting as proposed.

With respect to sub-advised funds, to prevent duplicative reporting, only one adviser should report information on Form PF with respect to that fund.[136] For reporting efficiency and to prevent duplicative reporting, if the adviser that completes information in section 7.B.1. of Schedule D to Form ADV with respect to any private fund is also required to file Form PF, the same adviser is responsible for reporting on Form PF with respect to that fund.[137] However, if the adviser that completes information on Schedule

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135 *See* Instruction 2 to Form PF. *See supra* note 117 for the definition of "related person."

136 Each adviser that meets the criteria for reporting on Form PF has an independent obligation to file the Form with respect to every fund it advises. *See* Advisers Act rule 204(b)-1(a); Instructions 1 and 3 to Form PF. However, when one adviser files Form PF with respect to a fund for a given reporting period, the other advisers are relieved of their obligation to file for that fund.

137 *See* Instruction 4 to Form PF. We have modified this instruction from the proposal to clarify who would report in the case that the adviser completing section 7.B.1 of Schedule D to Form ADV with respect to a particular private fund is an exempt reporting

D to Form ADV with respect to the private fund is not required to file Form PF (such as in the case of an exempt reporting adviser), then another adviser must report on that fund on Form PF.[138] If none of the advisers to a fund is required to file Form PF because they are all exempt reporting advisers or do not exceed the minimum reporting threshold, Instruction 4 to Form PF would not require any adviser to file the Form with respect to that fund. Commenters did not address this aspect of the proposal.

7. Exempt Reporting Advisers

Only private fund advisers registered with the SEC (including those that are also registered with the CFTC as CPOs or CTAs) must file Form PF.[139] As noted above, the Dodd-Frank Act created exemptions from SEC registration under the Advisers Act for advisers solely to venture capital funds and for advisers solely to private funds that in the aggregate have less than $150 million in assets under management in the United States.[140] We believe that Congress' determination to exempt these advisers from SEC registration indicates Congress' belief that regular reporting of detailed systemic risk information may not be necessary because they are sufficiently unlikely to pose this kind of risk.[141] After consultation with staff representing FSOC's members and in light of the

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adviser or does not meet the new minimum reporting threshold of $150 million in private fund assets under management.

138 *See* Instruction 4 to Form PF. *See supra* note 48 and accompanying text.

139 *See* Advisers Act rule 204(b)-1.

140 *See supra* note 53 and accompanying text.

141 *See* Senate Committee Report, *supra* note 5, at 74 ("The Committee believes that venture capital funds…do not present the same risks as the large private funds whose advisers are required to register with the SEC under this title. Their activities are not interconnected with the global financial system, and they generally rely on equity funding, so that losses

basic information that the SEC obtains from exempt reporting advisers on Form ADV, the SEC did not propose to extend Form PF reporting to these advisers.[142] Commenters that addressed this aspect of the proposal agreed that exempt reporting advisers should not be required to file Form PF, and we have adopted this approach as proposed.[143]

B. Frequency of Reporting

1. Annual and Quarterly Reporting

Most private fund advisers, including large private equity advisers and smaller private fund advisers, are required to complete and file Form PF only once per fiscal year.[144] Large hedge fund advisers and large liquidity fund advisers, on the other hand, must update information relating to their hedge funds or liquidity funds, respectively, each fiscal quarter.[145] Periodic reporting will permit FSOC to monitor periodically certain key information relevant to assessing systemic risk posed by these private funds on both an individual and aggregate basis. More frequent, quarterly reporting for large

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that may occur do not ripple throughout world markets but are borne by fund investors alone."). *See also* Exemptions Adopting Release, *supra* note 11.

142 *See* Implementing Adopting Release, *supra* note 11, for a discussion of the information exempt reporting advisers are required to provide on Form ADV.

143 *See* AIMA General Letter; Lone Star Letter. To the extent an exempt reporting adviser is registered with the CFTC as a CPO or CTA, the CFTC has proposed that the adviser would be obligated to file either Form CPO-PQR or CTA-PR, respectively.

144 *See* Instruction 9 to Form PF.

145 Even these advisers, however, need only update information regarding other types of funds they manage on an annual basis. For example, a large hedge fund adviser that also manages a small amount of liquidity fund and private equity fund assets must update information relating to its hedge funds each quarter but only needs to update information relating to its liquidity funds and private equity funds when it submits its fourth quarter filing. An adviser that is both a large hedge fund adviser and a large liquidity fund adviser must file quarterly updates regarding both its liquidity funds and hedge funds. *See* Instruction 9 to Form PF.

hedge fund and large liquidity fund advisers is necessary in order to provide FSOC with timely data to identify emerging trends in systemic risk.[146]

The filing requirements we are adopting differ from the proposal in two principal respects. First, the proposal would have required large private equity advisers to report on a quarterly, rather than annual, basis. Second, under the proposal, once an adviser became subject to quarterly reporting, it would have been required to update information with respect to all of its private funds each quarter (not just for the type of private fund that caused it to exceed the large adviser threshold).[147]

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146 *See* Proposing Release, *supra* note 12, at section II.C. We also noted in the Proposing Release that we understood hedge fund advisers already collect and calculate on a quarterly basis much of the information that Form PF requires relating to hedge funds. One commenter argued that this is only true with respect to the information required in sections 1a and 1b of Form PF. *See* comment letter of Fidelity Investments (Apr. 12, 2011) ("Fidelity Letter"); *see also* MFA Letter. We have taken these comments into account in determining to extend the reporting deadlines for hedge fund advisers, as discussed below in section II.B.2 of this Release. We note, however, that another commenter also stated that "Form PF for the most part... [requests] information that is part of, or should be part of, the existing risk management processes at the responding institutions," and as such "this information will either be something the adviser produces already, or arguably should." Comment letter of MSCI Inc. (submitted to the CFTC) (Apr. 11, 2011) ("MSCI Letter"). Commenters did not address the ability of liquidity funds to prepare and submit quarterly filings, and we continue to believe, as discussed in the Proposing Release, that most liquidity fund advisers collect on a monthly basis much of the information that we are requiring in section 3 of Form PF and that quarterly reporting should, as a result, be relatively efficient for these advisers.

147 The proposal also would have required reporting based on calendar quarters rather than the adviser's fiscal quarters. We have made this change because some advisers with quarterly updating obligations will now only need to update information about certain funds on an annual basis. The annual reporting is intended to align with typical end of fiscal year reporting activities, and requiring advisers to file separate annual and fourth quarter reports would impose additional burdens. We believe this change will, in practice, have little effect on the reporting (based on IARD data as of October 1, 2011, only about 2% of all registered advisers report a fiscal year ending in a month other than March, June, September or December, though the total may be slightly higher because IARD does not distinguish among, for instance, mid-month and end-of-month fiscal year ends).

A number of commenters responded to our proposal regarding the frequency of reporting. One agreed that quarterly reporting would be appropriate, and two others argued that advisers should report even more frequently because market conditions and portfolios can change rapidly.[148] On the other hand, a number of commenters disagreed with the proposal, suggesting instead that Large Private Fund Advisers should report no more than semi-annually.[149] These commenters argued that semi-annual reporting would reduce the burden to advisers while also giving regulators more time to analyze the data, and several compared Form PF to the FSA Survey, which has been conducted on a voluntary, semi-annual basis.[150] Another commenter stated that the generally illiquid portfolios of private equity funds fluctuate little in value throughout the year, in its view, making quarterly reporting unnecessary.[151]

After consultation with staff representing FSOC's members, we continue to believe that quarterly reporting is important to provide FSOC with meaningfully current information with respect to the hedge fund and liquidity fund industries and to allow FSOC to identify rapidly emerging trends among these types of funds.[152] Although some commenters suggested that the speed with which markets and portfolios change may warrant even more frequent reporting, we believe at this time that the additional benefit

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148 *See* CPIC Letter (supporting the proposal with respect to large private funds advisers); AFL-CIO Letter and AFR Letter (arguing for more frequent reporting).

149 *See*, *e.g.*, ABA Committees Letter; BlackRock Letter; Fidelity Letter; comment letter of Kleinberg, Kaplan, Wolff & Cohen, P.C. (submitted to the SEC) (Apr. 12, 2011) ("Kleinberg General Letter"); MFA Letter; SIFMA Letter; USCC Letter.

150 *See*, *e.g.*, ABA Committees Letter; Kleinberg General Letter.

151 *See* PEGCC Letter.

152 Moreover, we believe that quarterly reporting helps to discourage "window-dressing" around the reporting dates. *See infra* notes 285-292 and accompanying text.

to FSOC from reporting more often than once a quarter would not justify the additional burdens imposed on advisers.[153] On the other hand, we are also not convinced that less frequent (*e.g.*, semi-annual) reporting would provide sufficient, or sufficiently timely, information to enable FSOC to identify and respond to rapidly emerging trends. In addition, we believe that international approaches to private fund reporting may be shifting in favor of quarterly, rather than semi-annual, reporting.[154]

With respect to large private equity advisers, however, the SEC is persuaded that the generally illiquid nature of private equity fund portfolios means that trends emerge more slowly in that sector.[155] As a result, the proposal has been modified so that large private equity advisers are required to report information regarding private equity funds on an annual basis only.[156]

Fewer commenters addressed the frequency of reporting for smaller advisers. One commenter agreed that annual reporting would be appropriate for these advisers,[157] and several others argued that smaller advisers should report more frequently, proposing at least semi-annual filings.[158] Again, although we acknowledge the potential value of more frequent reporting from smaller private fund advisers, we are concerned about the

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153 *See supra* note 148. We also note that FSOC has the authority to direct OFR to gather additional data where systemic risk concerns merit the reporting. *See, e.g.*, sections 153 and 154 of the Dodd-Frank Act.

154 ESMA's proposed reporting template would impose quarterly reporting requirements on private fund advisers. *See* ESMA Proposal, *supra* note 33.

155 *See supra* note 151.

156 *See* Instruction 9 to Form PF.

157 *See* AIMA General Letter.

158 *See* AFL-CIO Letter; AFR Letter. *See also* MFA Letter (arguing that all advisers, large and small, should report on a semi-annual basis).

burden this would impose. At this time, we are not convinced that more frequent reporting from smaller private fund advisers would, from a systemic risk monitoring perspective, be justified by the value of the additional data.

As noted above, the requirements we are adopting also differ from the proposal in that even those advisers who must report on a quarterly basis are only required to do so with respect to the type of fund that caused them to exceed the reporting threshold. We are adopting this approach in part because these other funds will include private equity funds, venture capital funds and real estate funds, all of which are likely to have generally illiquid portfolios and for which we believe annual reporting is appropriate, as explained above. This approach also reflects the different implications for systemic risk that may be presented by different investment strategies.

2. Reporting Deadlines

Large private equity advisers and smaller private fund advisers have 120 days from the end of their fiscal years to file Form PF.[159] In contrast, large hedge fund advisers have 60 days from the end of each fiscal quarter, and large liquidity fund advisers have 15 days.[160] The deadlines we are adopting for large hedge fund advisers, large private equity advisers and smaller advisers are longer than the deadlines we

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159 *See* Instruction 9 to Form PF; Advisers Act rule 204(b)-1(a).

160 *See* Instruction 9 to Form PF. As discussed above, a large hedge fund adviser (or large liquidity fund adviser) that also manages other types of funds must file quarterly updates with respect to its hedge funds (or liquidity funds, as applicable) but only needs to update information regarding its other funds when it files its fourth quarter update. Such an adviser may comply with its filing obligations by initially filing a fourth quarter update that includes only information about its hedge funds (or liquidity funds, as applicable) within 60 days (or 15 days, as applicable) and then amending its filing within 120 days after the end of the quarter to include information about its other funds.

proposed. In particular, we have extended the deadline for large hedge fund advisers from 15 days to 60 days, the deadline for large private equity fund advisers from 15 days to 120 days and the deadline for smaller private fund advisers from 90 days to 120 days.[161]

The proposed deadline of 15 days for large hedge fund and private equity fund advisers attracted significant opposition. Commenters offered a number of reasons to extend the deadline, including that: (1) 15 days is not enough time to prepare and submit a report with reliably accurate data, particularly where the adviser must value illiquid fund assets;[162] (2) other SEC reporting requirements allow more time;[163] (3) the FSA Survey has allowed more time (approximately 30 to 45 days in the most recent surveys) and required less detail;[164] (4) the same personnel will be closing the books at the end of the quarter and completing Form PF;[165] and (5) the more current the information

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161 We noted in the Proposing Release that the proposed 90 day deadline would allow these advisers to file amendments at the same time as they file their Form ADV annual updating amendment, which may make certain aspects of the reporting more efficient, such as reporting assets under management. Proposing Release, *supra* note 12, at section II.C. We believe these efficiencies will still be realized because the reporting continues to be "as of" the same date as the annual reports on Form ADV and an adviser may still file on or after the date on which it files Form ADV.

162 *See, e.g.*, ABA Committees Letter; AIMA General Letter; BlackRock Letter; IAA Letter; MFA Letter; USCC Letter.

163 *See, e.g.*, ABA Committees Letter (noting that Forms N-SAR and N-Q, used by registered investment companies, allow 60 days); AIMA General Letter (pointing to Form 13F (allowing 45 days), Form 10-K (allowing at least 60 days), and Form 10-Q (allowing at least 40 days)); Fidelity Letter; Kleinberg General Letter; MFA Letter (pointing to the 120 days allowed for audited financial statements under the Advisers Act custody rule); TCW Letter.

164 *See, e.g.*, AIMA General Letter; IAA Letter.

165 *See, e.g.*, Kleinberg General Letter.

reported, the greater the consequences should it become public.[166] These commenters suggested alternatives that ranged from 45 to 120 days.[167] We understand from the comments, however, that the proposed reporting deadlines would be more problematic for some types of advisers than for others. For instance, commenters focusing on private equity advisers generally suggested longer deadlines than commenters focusing on hedge fund advisers, and the valuation of illiquid portfolios is likely to be a more common problem for private equity advisers.[168] Also, although a number of commenters addressed hedge fund advisers and private equity advisers, none commented specifically on whether liquidity fund advisers could meet the proposed deadline.

We are persuaded that longer deadlines are appropriate for large hedge fund advisers and large private equity fund advisers and that, with respect to large private equity fund advisers in particular, the work required to value the generally illiquid portfolios of private equity funds favors a substantially longer reporting deadline than

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166 *See, e.g.*, AIMA General Letter; Kleinberg General Letter. Some commenters also pointed to the Form's proposed signature page, which would have required advisers to certify that the information provided is "true and correct," arguing that this standard would be difficult to satisfy in 15 days. *See, e.g.*, AIMA General Letter. As discussed below, we are not adopting the proposed certification requirement. *See infra* notes 183-185 and accompanying text.

167 *See, e.g.*, AIMA General Letter (45 days); Akina Letter (120 days for private equity fund data); BlackRock Letter (120 days); CPIC Letter (45 days, at least initially); Fidelity Letter (preferably 90 days, but no less than 45 days); IAA Letter (90 days); Kleinberg General Letter (60 days); Lone Star Letter (60 days for private equity fund data); Merkl February Letter (four months for private equity fund data); MFA Letter (120 days); PEGCC Letter (at least 90 days for private equity fund data); Seward Letter (120 days); SIFMA Letter (120 days); TCW Letter (60 days); USCC Letter (120 days).

168 *Id.*

was proposed.[169] A few commenters favored a deadline for large hedge fund advisers longer than the one we are adopting, but several commenters indicated that a deadline shorter than the one we are adopting would be adequate.[170] We believe that our revised approach strikes an appropriate balance between the need to provide FSOC with timely data and the ability of these advisers to prepare and submit Form PF. We also believe it will reduce the burden of reporting for these advisers.

Fewer commenters addressed the proposed reporting deadline of 90 days for smaller advisers. One commenter supported the proposal,[171] but several argued that smaller advisers should have more than 90 days to prepare and submit their filings.[172] Several commenters noted that the Advisers Act custody rule allows advisers up to 120 days to distribute audited financial statements to investors when relying on the annual audit provision under that rule.[173] We believe that our revised deadline of 120 days will enable these advisers to benefit from the availability of financial statements and also help to avoid crowding advisers' calendars with end of year reporting obligations while at the same time providing FSOC with reasonably timely data.

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169 We note that many of the questions in section 4, which large private equity fund advisers must file, relate to information that should be available on the financial statements of their portfolio companies. By extending the deadline to 120 days for these advisers, we anticipate that the burden of reporting will be reduced because, in many cases, they will now be able to delay reporting until after receiving financial statements from their portfolio companies.

170 *See supra* note 167.

171 *See* AIMA General Letter.

172 *See, e.g.*, BlackRock Letter (120 days); MFA Letter (120 days); PEGCC Letter (150 days for private equity fund data).

173 *See, e.g.*, BlackRock Letter; MFA Letter; USCC Letter. *See also* Advisers Act rule 206(4)-2(b)(4).

3. Initial Reports

Newly registering private fund advisers are subject to the same Form PF reporting deadlines as currently registered advisers.[174] Advisers are not, however, required to file Form PF with respect to any period that ended prior to the effective date of their registrations. Accordingly, a smaller private fund adviser that registers during its 2013 fiscal year must file Form PF within 120 days following the end of its 2013 fiscal year. It would not, however, need to file Form PF for its 2012 fiscal year. Similarly, a large hedge fund adviser that registers during its third fiscal quarter must file Form PF within 60 days following the end of that quarter but need not file for the preceding fiscal quarter.[175]

We have extended the deadlines for initial filings from the 15 days that we proposed. One commenter argued that the proposed deadline would be too short and suggested 90 days instead.[176] We believe the revised initial filing deadlines are more consistent with the deadlines for updating Form PF discussed above in section II.B.2 of this Release.

4. Transition Filings, Final Filings and Temporary Hardship Exemptions

An adviser must file Form PF to report that it is transitioning to only filing Form PF annually with the Commissions or to report that it no longer meets the

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174 *See* Advisers Act rule 204(b)-1(a); *supra* section II.B.2 of this Release.

175 Whether an adviser is a large hedge fund or large liquidity fund adviser would be determined as of the date specified in Form PF, not the date of registration. When filing an initial Form PF, a large hedge fund or large liquidity fund adviser that also manages other types of private fund may rely on the instructions in the Form allowing it to delay updating information regarding these other fund types when filing an update.

176 *See* AIMA General Letter.

requirements for filing Form PF no later than the last day on which the adviser's next Form PF update would be timely.[177] This allows us to determine promptly whether an adviser's discontinuance in reporting is due to it no longer meeting the form's reporting thresholds as opposed to a lack of attention to its filing obligations. Advisers may also avail themselves of a temporary hardship exemption in a similar manner as with other SEC filings if they are unable to file Form PF electronically in a timely manner due to unanticipated technical difficulties.[178] No commenters addressed the proposed transition filings, final filings or temporary hardship exemption, and we are adopting them as proposed.

C. Information Required on Form PF

The questions contained in Form PF reflect relevant requirements and considerations under the Dodd-Frank Act, consultations with staff representing FSOC's members, and the Commissions' experience in regulating those private fund advisers that are already registered with the Commissions. As discussed above, with respect to hedge fund advisers in particular, the information collected on Form PF is also broadly based on the guidelines initially developed in the FSA Survey and the IOSCO report on hedge fund oversight, and many of the more detailed items are similar to questions proposed to be

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177 *See* Instruction 9 to Form PF.

178 *See* Advisers Act rule 204(b)-1(f); Instruction 14 to Form PF. The adviser would complete and file on paper Item A of section 1a and section 5 of Form PF, checking the box in section 1a indicating that it is requesting a temporary hardship exemption. The adviser must file any request for a temporary hardship exemption no later than one business day after the electronic Form PF filing was due. The adviser must then submit the filing that is the subject of the Form PF paper filing in electronic format with the Form PF filing system no later than seven business days after the filing was due.

included in ESMA's reporting template.[179] Form PF has been designed to collect information to assist FSOC in monitoring and assessing systemic risks that private funds may pose, as discussed in section II.A above.

Commenters' reactions to the scope of Form PF varied, with some proposing further enhancements and others arguing that the proposed reporting is excessive. Commenters arguing for expanded reporting recommended additional questions about counterparty exposures and short selling or suggested having all advisers complete the entire form.[180] In contrast, critics of the proposal argued that information required on Form PF would be unduly burdensome to provide or is available to regulators from other sources.[181] A few commenters who objected to other aspects of the proposal recommended adding several questions that were originally proposed on Form ADV.[182] Although this would expand the Form, these commenters believed that these questions, which relate to valuation, beneficial ownership and the identity of service providers, would require competitively sensitive or proprietary information and would be more appropriately reported confidentially on Form PF.

As discussed in greater detail below, Form PF, as adopted, addresses the concerns of many commenters with changes from the proposal that we believe will significantly reduce the burden of reporting and clarify how commenters are expected to respond. At

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179 *See supra* section I.B of this Release.

180 *See*, *e.g.*, AFL-CIO Letter; AFR Letter; Merkl February Letter; MSCI Letter; comment letter of Plexus Consulting Group (Feb. 28, 2011). *See also supra* note 76 and accompanying text.

181 *See*, *e.g.*, AIMA General Letter; IAA Letter; Olympus Letter; PEGCC Letter. *See infra* note 309 and accompanying text.

182 *See* IAA Letter; MFA Letter; Seward Letter.

the same time, the final Form preserves much of the information that the proposal would require. Our revised approach is intended to respond to industry concerns while still providing FSOC the information it needs to monitor systemic risk across the private fund industry.

Two of the changes we are making, in particular, illustrate this revised approach. The first is the removal of the proposed certification language. This would have required an authorized individual to affirm "under penalty of perjury" that the statements made in Form PF are "true and correct."[183] This certification was borrowed from the SEC's existing Advisers Act reporting form, Form ADV. However, a number of commenters expressed concern that such a standard would be inappropriate for Form PF because the Form requires advisers to provide estimates and exercise significant judgment in preparing responses.[184] In consideration of the nature of the information required on Form PF, we are persuaded that a certification is unnecessary and that a signature

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183 *See* Question 2 and Instruction 11 to Form PF. If the adviser is also registered with the CFTC as CPO or CTA, the signature page also requires the signatory to acknowledge that misstatements or omissions of material fact on Form PF constitute a violation of the CEA. This acknowledgement is included simply to remove any doubt created by the filing of the Form through the SEC rather than directly with the CFTC, which is merely a matter of convenience for advisers.

184 *See*, *e.g.*, ABA Committees Letter; AIMA General Letter; Kleinberg General Letter; MFA Letter; PEGCC Letter. Some of these commenters also saw the certification standard and the reporting deadlines as related issues, arguing that the more quickly advisers are required to report, the less confidence they will have in their estimates. *See*, *e.g.*, BlackRock Letter; Fidelity Letter; PEGCC Letter; SIFMA Letter; USCC Letter. As discussed above in section II.B.2 of this Release, we have also extended the proposed filing deadlines. Several commenters compared Form PF to other SEC forms and suggested that we either require just a signature without a certification or that we use a less stringent standard, such as good faith. *See* MFA Letter (pointing to the certification in the SEC's Schedule 13G). *See also* ABA Committees Letter (comparing Form PF to other SEC forms, including Form N-SAR, Form N-Q, Schedule 13D and Schedule 13G); AIMA General Letter (pointing to Schedule 13G); BlackRock Letter; Kleinberg General Letter.

confirming that the Form is filed with proper authority is sufficient.[185]

The second change is to increase the ability of advisers to rely on their internal methodologies when reporting on Form PF.[186] A number of commenters encouraged this approach, recommending "that the instructions to the Form be modified to confirm that advisers be able to rely on the same internal reporting procedures and practices when reporting on the Form that they would use when reporting to advisory clients, unless directly contradicted by the instructions."[187] The revised approach strikes an appropriate balance between easing the burden on advisers by allowing them to rely on their existing practices and ensuring that FSOC receives comparable data across the industry. This

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185 We note, however, that even absent the certification, a willful misstatement or omission of a material fact in any report filed with the SEC under the Advisers Act is unlawful. *See* section 207 of the Advisers Act. We have also added an instruction to the Form that clarifies when an adviser is required to amend its filing to correct an error. In particular, Instruction 16 to Form PF explains that an adviser is not required to update information that it believes in good faith properly responded to Form PF on the date of filing even if that information is subsequently revised for purposes of the adviser's recordkeeping, risk management or investor reporting (such as estimates that are refined after completion of a subsequent audit). The instruction also explains that large hedge fund advisers and large liquidity fund advisers that comply with their fourth quarter filing obligations by submitting an initial filing followed by an amendment in accordance with Instruction 8 to Form PF will not be viewed as affirming responses regarding one fund solely by providing updated information regarding another fund at a later date.

186 *See* Instruction 15 to Form PF. As noted in the instruction, we would expect reporting on Form PF to be consistent with information the adviser uses for internal and investor reporting purposes. Methodologies also must be consistently applied, and to the extent we have indicated how an adviser should respond to a question, the answer should be consistent with our instructions. In addition to this general instruction, we have increased the ability of advisers to rely on their own methodologies with a number of specific changes throughout the Form, including permitting advisers to report performance using their existing practices, allowing flexibility in reporting interest rate sensitivities and changing the frequency and substance of reporting for large private equity advisers. *See, e.g.*, *infra* notes 202, 241-242, 247-248 and 258-260 and accompanying text and section II.C.4.

187 BlackRock Letter. *See also* IAA Letter; MFA Letter; PEGCC Letter; SIFMA Letter; TCW Letter.

change is intended, together with the removal of the certification, to clarify that Form PF does not require the time or expense involved in, for instance, an audit of the information included on Form PF, and we anticipate that these changes will reduce the burden that many advisers incur in completing the Form.[188]

The information that Form PF requires and the changes made from the proposal are discussed in detail below.

1. Section 1 of Form PF

Each adviser required to file Form PF must complete all or part of section 1. This section of the Form is divided into three parts: section 1a requires information regarding the adviser's identity and assets under management, section 1b requires limited information regarding the size, leverage and performance of all private funds subject to the reporting requirements, and section 1c requires additional basic information regarding hedge funds. We are adopting Form PF with several changes to the information that advisers are required to report in section 1. These changes, which are discussed in detail below, are intended to respond to industry concerns while still providing FSOC the information it needs to monitor systemic risk across the private fund industry. In general, we expect that these changes will reduce the burden of responding to the Form and more closely align the Form with ESMA's proposed reporting template.

a. Section 1a of Form PF

Item A of section 1a seeks identifying information about the adviser, such as its name and the name of any of its related persons whose information is also reported on the

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188 If audited information is available at the time an adviser files Form PF, we would of course expect responses to Form PF to be consistent with that audited information.

adviser's Form PF. The adviser will also be required to provide its large trader identification number, if any.[189] The addition of the large trader identification number will enhance the value of Form PF information by allowing it to be quickly and accurately linked to other information that may be available to the SEC while imposing little additional burden. Section 1a also requires basic aggregate information about the private funds managed by the adviser, such as the portion of gross (*i.e.*, regulatory) and net assets under management attributable to certain types of private funds.[190] This identifying information will assist us and FSOC in monitoring the amount of assets managed by private fund advisers and the general distribution of those assets among various types of private funds.[191] This information also provides data about the size of the adviser, the nature of the adviser's activities and the extent to which assets are managed rather than owned, which are factors that FSOC must consider in making a

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189 *See* Question 1 on Form PF.

190 *See* Question 3 on Form PF. This question requires the adviser to report the portion of its assets under management that are attributable to hedge funds, liquidity funds, private equity funds, real estate funds, securitized asset funds, venture capital funds, other private funds, and funds and accounts other than private funds. We have modified the instructions to Question 3 to improve their consistency and to respond to a commenter's request for clarification regarding the meaning of "funds and accounts other than private funds." *See* MFA Letter. We have also determined not to adopt a proposed question that would have required advisers to report their aggregate gross and net regulatory assets under management because this information can be derived from the data reported in Question 3. *See* the Proposing Release, *supra* note 12, for the proposed Question 3 on Form PF.

191 Question 4 in section 1a of Form PF also permits an adviser to explain any assumptions it made in responding to Form PF. This question is optional. One commenter expressed support for "providing space for managers to describe any assumptions they make in responding to a question," and we are adopting this question substantially as proposed. *See* MFA Letter.

determination to designate a nonbank financial company for FRB supervision under the Dodd-Frank Act.[192]

b. Section 1b of Form PF

Section 1b of Form PF elicits certain identifying and other basic information about each private fund the adviser manages. The adviser generally must complete a separate section 1b for each private fund.[193] This section of the Form requires reporting of each private fund's gross and net assets and the aggregate notional value of its derivative positions.[194] It also requires basic information about the fund's borrowings, including a breakdown showing whether the creditor is based in the United States and whether it is a financial institution.[195] Advisers must also report the percentage of the

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192 *See* section 113(a) of the Dodd-Frank Act; FSOC Second Notice, *supra* note 6.

193 However, if the adviser elects to report on an aggregated basis regarding the funds comprising a master-feeder arrangement or a parallel fund structure, it would only file a single section 1b for the master fund in the master-feeder arrangement or for the largest fund in the parallel fund structure. We have modified the approach to aggregation of master-feeder arrangements and parallel fund structures to allow advisers more flexibility in determining how to report. *See* Instruction 5 to Form PF. This change is discussed in greater detail below in section II.C.5 of this Release.

194 *See* Questions 8, 9 and 13 on Form PF. With respect to Question 13 and similar questions regarding the value of derivatives, the Form requires the adviser to report the gross notional value of its funds' derivative positions, except that options must be reported using their delta adjusted notional value. *See* Instruction 15 to Form PF. In contrast, Questions 8 and 9, and similar questions that refer to gross asset value or net asset value, require valuations based on the instruction in Form ADV for calculating regulatory assets under management. *See* definitions of "gross asset value" and "net asset value" in the Glossary to Form PF.

195 *See* Question 12 on Form PF. One commenter suggested that the amount of borrowings should be netted where a private fund is both a lender to and a creditor of a counterparty. *See* MFA Letter. The commenter's approach would, however, obscure the total amount of leverage the fund has incurred, and we have clarified that such amounts should not be netted. Also, in response to this commenter, we have modified the instructions to clarify that collateral should not be netted against borrowings. We have also modified this question, and other questions on the Form requiring a breakdown of creditor types, to split the non-financial institution category into U.S. and non-U.S. creditors. This change

fund's equity held by the five largest equity holders, which provides information about the concentration of the fund's investor base.[196] Two new questions, which we have added in connection with other changes to the Form, also require the value of the fund's investments in other private funds and of the parallel managed accounts managed alongside the fund.[197]

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is intended to increase the usefulness of this data for the FRB's flow of funds report, which is an important tool for evaluating trends in and risks to the U.S. financial system. *See infra* note 475.

We proposed that advisers completing section 1b also report the identity of, and amount owed to, each creditor to which the fund owed an amount equal to or greater than 5 percent of the fund's net asset value as of the reporting date. *See* the Proposing Release, *supra* note 12, for the proposed Question 10 on Form PF. This question has been moved to section 2b of the Form so that only large hedge fund advisers must provide this information. This change is intended to respond to commenter concerns that completing this question will be burdensome but also preserve information regarding interconnectedness that may be important to FSOC's monitoring of systemic risk among large hedge funds. *See*, *e.g.*, PEGCC Letter.

196 *See* Question 15 on Form PF. For purposes of this question and Question 16 on Form PF, beneficial owners are persons who would be counted as beneficial owners under section 3(c)(1) of the Investment Company Act or who would be included in determining whether the owners of the fund are qualified purchasers under section 3(c)(7) of that Act. (15 U.S.C. 80a-3(c)(1) or (7)). The proposal would have required that advisers report the number of beneficial owners of the fund. However, we are not adopting this question because, as a result of our revised approach to reporting on parallel managed accounts, this information will largely duplicate information collected on Form ADV, and we do not believe that receiving updated responses on a quarterly basis from large hedge fund advisers and large liquidity fund advisers is necessary with respect to this information. *See infra* section II.C.5 of this Release. *See also* the Proposing Release, *supra* note 12, for the proposed Question 12(a) on Form PF; Question 13 of section 7.B.1. of Schedule D to Form ADV.

197 *See* Questions 10 and 11 on Form PF. Question 10, which asks for the value of the fund's investments in other private funds, has been added because our expanded Instruction 7 otherwise allows these investments to be disregarded on Form PF and it is important that FSOC have a basic measure of the extent of assets not otherwise reflected on the Form. This will also serve as a measure of interconnectedness among private funds. *See supra* notes 128 and 131 and accompanying text for a discussion of Instruction 7. Question 11, relating to the value of parallel managed accounts, has been added for similar reasons. *See infra* section II.C.5 of this Release for a discussion of our revised approach to reporting on parallel managed accounts.

Section 1b also requires that advisers report in response to Question 17 the performance of each fund, both on a gross basis and net of management fees and incentive fees and allocations. Advisers must provide performance information that is consistent with the performance results they report to investors (or use internally, if not reported to investors). Advisers are required, at a minimum, to report annual performance results for the fund's most recently completed fiscal year but only need to report monthly and quarterly performance information if that information is already being calculated for the fund.

Question 17 has been modified from the proposal in response to commenter concerns regarding the burden of providing performance results in the form proposed.[198] In particular, it omits the requirement to report the change in net asset value, allows advisers to report performance gross and net of management fees and incentive fees and allocations (rather than gross and net of incentive fees and allocations only) and makes reporting of monthly and quarterly performance mandatory only for those funds for which advisers are already calculating performance results with that frequency. Commenters were concerned primarily that the proposed instructions to this question would require advisers to calculate performance in a manner different from that used for investor reporting purposes or more frequently than is their current practice.[199] A number of commenters explained that funds with illiquid portfolios, such as private equity funds, typically do not calculate performance on a monthly (and in many cases,

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198 *See infra* notes 199 and 200.

199 *See, e.g.*, ABA Committees Letter; MFA Letter (recommending that "the Form be revised to request (i) gross performance and (ii) performance net of all fees" and suggesting that advisers be permitted to report what they report to private fund investors).

even quarterly) basis and that calculating performance more frequently would impose a significant burden on these advisers.[200] As discussed above, we are persuaded that trends emerge more slowly in private funds having illiquid portfolios, meaning that developments in these funds may be tracked using information reported on a less frequent basis.[201] We believe that the revised approach, which allows advisers to rely on their existing procedures for calculating and reporting fund performance, significantly reduces the burden of responding to this question but will nonetheless yield valuable information for FSOC.[202]

We have also added to section 1b two questions that the SEC originally proposed as part of the expanded private fund reporting in Form ADV.[203] The first, Question 14, requires that advisers report the assets and liabilities of each fund broken down using categories that are based on the fair value hierarchy established under U.S. generally accepted accounting principles ("GAAP").[204] The second, Question 16, requires that

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200 *See*, *e.g.*, ABA Committees Letter; IAA Letter; Merkl February Letter; MFA Letter; PEGCC Letter; SIFMA Letter; TCW Letter.

201 *See supra* text accompanying note 156.

202 *See* Question 17 on Form PF. *See also* Proposing Release, *supra* note 12, at text accompanying n. 115 for a discussion of potential uses for this data.

203 *See* Questions 14 and 16 on Form PF.

204 Advisers must report this information annually (or on their fourth quarter updates, in the case of large hedge fund and large liquidity fund advisers). This question will provide information indicating the illiquidity and complexity of a fund's portfolio and the extent to which the fund's value is determined using metrics other than market mechanisms. In a recent rulemaking release, FSOC identified this fair value categorization as the type of information that may be important for assessing liquidity risk and maturity mismatch, one factor in determining whether a nonbank financial company may pose systemic risk. *See* FSOC Second Notice, *supra* note 6. *See also Rules Implementing Amendments to the Investment Advisers Act of 1940*, Investment Advisers Act Release No. 3110 (Nov. 19, 2010), 75 FR 77052 (Dec. 10, 2010) ("Implementing Proposing Release") for the proposed version of Form ADV, Part 1A, section 7.B.(1)A. of Schedule D, question 12.

advisers provide the approximate percentage of each fund beneficially owned by certain types of investors.[205] As discussed in the Implementing Adopting Release, the SEC determined not to adopt these questions on Form ADV in response to commenter concerns that they would result in the public disclosure of competitively sensitive or proprietary information.[206] We have added these questions to Form PF (with the modifications discussed below) because, as the SEC explained in the Implementing Adopting Release, this information may be important to FSOC's systemic risk monitoring activities and to our investor protection mission.[207]

Commenters responding to these questions as proposed on Form ADV argued that they would be difficult or burdensome to complete. With respect to Question 14, commenters argued that some private funds – especially non-U.S. funds – do not use generally accepted accounting principles (whether U.S. or international) or obtain audited financial statements, making the requirement to report a breakdown of fair values

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See also FASB ASC 820-10-50-2b.

We have modified this question from the proposal to expressly include definitions for Levels 1, 2 and 3 of the hierarchy. This change is intended to minimize ambiguity for advisers that do not utilize GAAP or another international accounting standard that requires the contemplated breakdown of assets and liabilities. Advisers that already prepare this breakdown for financial reporting purposes should respond to this question using the fair value hierarchy established under the applicable accounting standard.

205 *See* the Implementing Proposing Release for the proposed version of Form ADV, Part 1A, section 7.B.(1)A. of Schedule D, question 17.

206 *See* Implementing Adopting Release, *supra* note 11, at nn. 246-247. Information filed on Form ADV is made available to the public through the Investment Adviser Public Disclosure (IAPD) website. In contrast, information filed on Form PF will generally remain confidential. *See infra* section II.D of this Release.

207 *Id*. Several commenters responding to the Proposing Release also encouraged us to move these questions from Form ADV to Form PF. *See* IAA; MFA Letter; Seward Letter.

potentially costly.[208] We understand, however, that the group of funds not using some form of generally accepted accounting standard is relatively small and that most private funds already utilize GAAP or other international accounting standards that require the contemplated breakdown of assets and liabilities.[209] In addition, funds are not required to adopt GAAP for these purposes, and Question 14 does not require that the *valuations* within the breakdown of assets and liabilities be audited, or even determined in accordance with GAAP. For instance, an adviser could rely on the procedure for

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208 Comment letter of the American Bar Association, Federal Regulation of Securities Committee and Private Equity and Venture Capital Committee (Jan. 31, 2011) (commenting on the Implementing Proposing Release, *supra* note 204) ("ABA Committees Implementing Proposal Letter"); comment letter of the Alternative Investment Management Association (Jan. 24, 2011) (commenting on the Implementing Proposing Release, *supra* note 204) ("AIMA Implementing Proposal Letter"); comment letter of Dechert LLP (Jan. 24, 2011) (commenting on the Implementing Proposing Release, *supra* note 204); comment letter of the Investment Adviser Association (Jan. 24, 2011) (commenting on the Implementing Proposing Release, *supra* note 204) ("IAA General Implementing Proposal Letter"); comment letter of Katten, Muchin, Rosenman, LLP (Jan. 24, 2011) (commenting on the Implementing Proposing Release, *supra* note 204); comment letter of George Merkl (Jan. 25, 2011) (commenting on the Implementing Proposing Release, *supra* note 204); comment letter of the National Venture Capital Association (Jan. 24, 2011) (commenting on the Implementing Proposing Release, *supra* note 204). Some of these commenters further contended that investors would bear any new audit costs or that advisers would not necessarily have audited numbers within 90 days after fiscal year end, when Form ADV is due. *See*, *e.g.*, ABA Committees Implementing Proposal Letter; AIMA Implementing Proposal Letter; IAA General Implementing Proposal Letter.

209 *See*, *e.g.*, Implementing Proposing Release, *supra* note 204, at n. 56. Indeed, even in the context of this rulemaking, the Managed Funds Association suggested that we use a GAAP standard to measure advisers' assets, asserting that "GAAP information is regularly reported across the industry and is a data point that most managers track in the ordinary course...." MFA Letter. Others advisers may use international accounting standards requiring substantially similar information. In the Implementing Adopting Release, the SEC estimated that only about 3% of registered advisers have at least one private fund client that may not be audited. *See* Implementing Adopting Release, *supra* note 11, at nn. 634-636 and accompanying text.

calculating fair value that is specified in a private fund's governing documents.[210] As a result, we are not convinced that the aggregate burden attributable to this reporting is unreasonable or even as significant as some commenters contend. The question has, however, been modified from the proposal to require a breakdown only by category and not by class.[211] For advisers that do not already prepare this breakdown for financial reporting purposes, this revised approach will significantly reduce the work required to respond to this question.[212] Such advisers may, nevertheless, incur additional costs to complete this question, and we are sensitive to these costs. We believe, however, that this question will provide valuable information for FSOC's systemic risk monitoring activities and our investor protection mission and that the associated burden is warranted.[213]

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210 The fair valuation process need not be the result of a particular mandated procedure and the procedure need not involve the use of a third-party pricing service, appraiser or similar outside expert. The fund's governing documents may provide, for example, that the fund's general partner determines the fair value of the fund's assets. We would, however, expect that an adviser that calculates fair value in accordance with GAAP or another basis of accounting for financial reporting purposes will also use that same basis for purposes of determining the fair value of its assets and liabilities for this purpose.

This question has been modified from the proposal to include a column titled "cost-based" for those assets and liabilities valued on the fund's financial statements using a measurement attribute other than fair value. This change recognizes that, even among advisers that already prepare a similar fair value breakdown for financial reporting purposes in accordance with GAAP, some assets and liabilities are not accounted for at fair value and, therefore, would not be included in the fair value hierarchy disclosures.

211 In other words, although an adviser will need to provide the fund's aggregate assets and liabilities categorized as Level 1, 2 or 3, it will not need to indicate the types of assets and liabilities in each of those categories.

212 In addition, for advisers that already prepare this breakdown for financial reporting purposes, this revised approach will reduce the amount of information that needs to be re-entered on Form PF.

213 *See supra* note 204 for a discussion of potential uses for this data.

Commenters also expressed concern regarding the burden of reporting the types of beneficial owners investing in each fund, as required in Question 16.[214] One of these commenters noted, for instance, that many advisers either do not have this information or keep this information on a basis different from that set out in the Form.[215] We believe, however, that many advisers to private funds are already collecting some of this beneficial ownership data as part of their processes for analyzing compliance with exemptions under the Investment Company Act and the Securities Act of 1933.[216] To the extent this information is not currently collected, we do not anticipate that adding this to the information advisers already routinely collect from fund investors will impose a significant burden. We acknowledge, however, that advisers managing funds with securities outstanding prior to the adoption of Form PF would have to take additional steps in order to obtain this information because the investor diligence process will already have been completed. As a result, with respect to beneficial interests outstanding prior to March 31, 2012, that have not been transferred on or after that date, advisers may respond to Question 16 using good faith estimates based on data available to them without making additional inquiries of investors.

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214 Comment letter of Debevoise & Plimpton, LLP (Jan. 24, 2011) (commenting on the Implementing Proposing Release, *supra* note 204) ("Debevoise Implementing Proposal Letter"); IAA General Implementing Proposal Letter; comment letter of Shearman & Sterling, LLP (Jan. 24, 2011) (commenting on the Implementing Proposing Release, *supra* note 204) ("Shearman Implementing Proposal Letter"). These commenters argued that advisers may have difficulty obtaining the required information for certain types of funds, particularly for funds established before the adoption of the reporting requirement.

215 *See* IAA General Implementing Proposal Letter (stating that the reporting would require "significant system enhancements").

216 15 U.S.C. 77a.

Question 16 has also been modified by adding a row for non-U.S. investors about which the adviser does not have and cannot reasonably obtain beneficial ownership information.[217] This change acknowledges that obtaining beneficial ownership information about certain non-U.S. investors may be difficult for some advisers and ameliorates that burden by allowing advisers to report only the size of the ownership interest about which data is not available. We have also modified from the proposal some of the other categories in this question based on our consultations with staff representing FSOC's members. In particular, we have split out categories regarding individuals and pension plans to obtain a slightly more granular breakdown and added a category for sovereign wealth funds and foreign official institutions. We intend these changes to increase the usefulness of this data for the FRB's flow of funds report, a tool that is used for evaluating trends in and risks to the U.S. financial system.[218]

The information that section 1b requires is designed to allow FSOC to monitor certain systemic trends for the broader private fund industry, such as how certain kinds of private funds perform and exhibit correlated performance behavior under different economic and market conditions and whether certain funds are taking significant risks that may have systemic implications. It is also intended to allow FSOC to monitor borrowing practices across the private fund industry, which may have interconnected

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217 An adviser may only report in this category beneficial ownership interests that are held through a chain involving one or more third-party intermediaries. If the beneficial owner has, for instance, simply interposed a wholly-owned holding company or trust as the legal owner, the interest would need to be reported in one of the other categories of beneficial owner.

218 *See infra* note 475. *See also* Flow of Funds Accounts of the United States, *available at* http://www.federalreserve.gov/releases/z1/.

impacts on banks and thus the broader financial system. Question 14, which requires that advisers report the assets and liabilities of each fund broken down using categories that are based on the fair value hierarchy established under GAAP, will provide information indicating the illiquidity and complexity of a fund's portfolio and the extent to which the fund's value is determined using metrics other than market mechanisms. In a recent rulemaking release, FSOC identified this fair value categorization as the type of information that may be important for assessing liquidity risk and maturity mismatch, one factor in determining whether a nonbank financial company may pose systemic risk.[219] Finally, as noted above, certain of the information that section 1b requires is designed for use in the FRB's flow of funds report, a tool that is used for evaluating trends in and risks to the U.S. financial system.[220]

c. Section 1c of Form PF

Section 1c is the final part of section 1 and requires advisers to report information regarding the hedge funds they manage, if any. This information includes each fund's investment strategies[221] and the percentage of the fund's assets managed using high-

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219 *See supra* note 204.

220 *See supra* note 218 and accompanying text.

221 *See* Questions 19 and 20 on Form PF. One commenter, although advising caution in using strategy data to analyze industry trends, asserted that the reporting could provide valuable information about emerging systemic risk. *See* MSCI Letter ("a buildup of assets in one or a set of related strategies should cause the FSOC to question the market's capacity to support such a strategy..." and create "conditions where crowded trades could be unwound quickly, with a systemic impact."). Another commenter suggested that we revise the question to allow reporting as of the end of the reporting period rather than over the course of the period and to permit advisers to report based on capital allocation rather than net asset value. *See* MFA Letter. We have revised the instructions to permit both these options. We have, however, also retained the requirement to report based on

frequency trading strategies.[222] Advisers must also report each hedge fund's significant counterparty exposures (including identity of counterparties).[223] In response to comments, we have modified the questions regarding counterparty exposures to clarify instructions and to reduce the reporting burden by more closely aligning the requirements with information already determined in connection with many contractual trading arrangements.[224]

Finally, section 1c requires information regarding each hedge fund's trading and clearing practices in Question 24 and activities conducted outside the securities and derivatives markets in Question 25. Some commenters supported the reporting required in Question 24.[225] However, one commenter expressed concern that the question as proposed would require burdensome manual aggregation.[226] In response, we have simplified this question by requiring a less detailed breakdown, removing the sub-classes

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percentage of net asset value because we believe this will provide valuable information regarding leverage.

222 *See* Question 21 on Form PF. Some commenters suggested removing this question because, in their view, it would not provide information relevant to systemic risk assessment. *See, e.g.*, AIMA General Letter; MFA Letter. This information may, however, be important to understanding how hedge funds interact with the markets and their role in providing trading liquidity. We have modified the instructions to this question to make it easier for advisers to determine whether a particular fund is using a relevant strategy.

223 *See* Questions 22 and 23 on Form PF.

224 *See* MFA Letter. Specifically, these questions have been modified to (i) clarify that exposure should be mark-to-market exposure (rather than potential exposure), (ii) narrow the conditions under which affiliates are treated as a single counterparty group in order to track legal and contractual arrangements among the parties, (iii) focus on counterparties generally (rather than just trading counterparties), (iv) reference exposures before taking into account collateral postings and (v) be less prescriptive regarding the treatment of assets in custody and unsettled trades.

225 *See* AFL-CIO Letter; AFR Letter.

226 *See* MFA Letter.

of securities and derivatives included in the proposal. We expect that, by requiring less refinement in the categories of investments, these changes will reduce the burden of responding to this question. The revisions also align this question with the similar questions in the FSA Survey and ESMA's proposed reporting template.[227]

The information required in section 1c is designed to enable FSOC to monitor systemic risk that could be transmitted through counterparty exposure, track how different strategies are affected by and correlated with different market stresses, and follow the extent of private fund activities conducted away from regulated exchanges and clearing systems. This information could be important to understanding interconnectedness, which relates to the factors that FSOC must consider in making a determination to designate a nonbank financial company for FRB supervision under the Dodd-Frank Act.[228]

Several commenters agreed that some or all of the information required in section 1c would be valuable.[229] For instance, one commenter, referring to the counterparty information, argued that "[f]rom a systemic risk perspective, this is the most relevant information on the form, as it goes to the heart of the issue of connectivity."[230] Some of these questions, including those about significant trading counterparty exposures and trading and clearing practices, are based on the FSA Survey, and some of the changes from the proposal discussed above more closely align this section with the FSA Survey

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227 *See* ESMA Proposal, *supra* note 33.

228 *See* section 113(a) of the Dodd-Frank Act; FSOC Second Notice, *supra* note 6.

229 *See* AFL-CIO Letter; AFR Letter; MSCI Letter.

230 *See* MSCI Letter; *infra* note 274.

and ESMA's proposed reporting template, which will promote international consistency in hedge fund reporting.[231]

2. Section 2 of Form PF

A private fund adviser must complete section 2 of Form PF if it had at least $1.5 billion in hedge fund assets under management as of the end of any month in the prior fiscal quarter.[232] This section of the Form requires additional information regarding the hedge funds these advisers manage, which we have tailored to focus on relevant areas of financial activity that have the potential to raise systemic concerns. This information corresponds to areas of potential concern that were identified in the Proposing Release and is designed to assist FSOC in monitoring and assessing the extent to which stresses at hedge funds could have systemic implications.

We are adopting Form PF with several changes to the information that advisers are required to report in section 2. These changes, which are discussed in detail below, are intended to respond to industry concerns while still providing FSOC the information it needs to monitor systemic risk across the hedge fund industry. In general, we expect that these changes will reduce the burden of responding to the Form and more closely align the Form with ESMA's proposed reporting template.

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231 For example, ESMA's proposed reporting template would ask for identification of the hedge fund's top five counterparties in terms of net credit exposure. It would also ask for estimates of the percentage of the fund's securities or derivatives traded on a regulated exchange versus over the counter and the percentage of the fund's derivatives and repos cleared by a central clearing counterparty versus bilaterally. In addition, the template would require advisers to identify a predominant trading strategy using categories similar to those on Form PF. *See* ESMA Proposal, *supra* note 33.

232 *See* Instruction 3 to Form PF; *supra* section II.A.4 of this Release.

a. Section 2a of Form PF

Section 2a requires certain aggregate information about the hedge funds the adviser manages. For example, Question 26 requires the adviser to report the value of assets invested (on a short and long basis) in different types of securities and commodities (*e.g.*, different types of equities, fixed income securities, derivatives, and structured products). One commenter acknowledged the importance of collecting this information, agreeing that it "could feed a variety of possible systemic risk indices."[233] Some commenters, however, expressed concern regarding the amount of detail required in this question,[234] and the commenter who generally supported this question nonetheless thought the asset classes placed too much emphasis on asset backed securities when compared with other asset classes.[235] In response, the amount of detail regarding asset backed securities has been reduced so that the adviser need only provide a breakdown of mortgage backed securities, asset backed commercial paper, collateralized debt and loan obligations, other asset backed securities and other structured products.[236] We continue

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233 MSCI Letter.

234 *See, e.g.*, ABA Committees Letter; MFA Letter.

235 *See* MSCI Letter.

236 This question has also been modified to separate foreign exchange derivatives used for investment from those used for hedging in response to a comment arguing that the proposed category should exclude foreign currency hedges. *See* MFA Letter. We have also added a category for physical real estate, which was not included in the FSA Survey but has been added in ESMA's proposed reporting template, in order to increase international consistency. *See* ESMA Proposal, *supra* note 33; *see also supra* note 31. In addition, following consultation with staff representing FSOC's members, we have separated investments in money market funds from other types of cash management funds and deposits from other types of cash equivalents. These changes are intended to provide additional detail regarding how cash equivalents are held because, at times of economic stress, these forms of holdings may have different implications for systemic risk.

to believe, however, that the remaining detail in this question is justified by the potential value of this information to FSOC's systemic risk monitoring activities.[237] One commenter suggested that, instead of the proposed categories of assets, we allow advisers to report based on GAAP classifications under FAS 157.[238] We do not believe this is a workable alternative because FAS 157 does not employ a standard set of asset classes, and the value of this information depends in part on the ability of regulators to make comparisons across funds.[239] We also believe that our approach is more consistent with international hedge fund reporting standards.[240]

Question 26 also requires the adviser to report the duration, weighted average tenor or 10-year bond equivalent of fixed income portfolio holdings (including asset backed securities). This differs from the proposal, which would have required all advisers to report duration. We are giving advisers the option of instead reporting weighted average tenor or 10-year bond equivalents because we understand from comments received that advisers use a wide range of metrics to measure interest rate sensitivity.[241] We expect that this revised approach will reduce the burden of reporting because advisers will generally be able to rely on their existing practices when providing this information. This approach may limit the ability of regulators to make comparisons

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237 *See* Proposing Release, *supra* note 12, at text accompanying n. 120 for a discussion of potential uses for this data.

238 *See* MFA Letter (this comment letter refers only to GAAP categories, but the commenter clarified on a call with staff that it was referring to the classifications under FAS 157).

239 We note that nothing would prevent an adviser from relying on its classifications of assets for financial reporting purposes when completing Form PF to the extent that asset classes overlap.

240 *See* FSA Survey; ESMA Proposal, *supra* note 33.

241 *See* ABA Committees Letter; MFA Letter.

across advisers but will still yield valuable information about sensitivities to interest rate changes.[242]

Question 27 requires the adviser to report the value of turnover in certain assets classes (including listed equities, corporate bonds, sovereign bonds and futures) in the hedge funds' portfolios during the reporting period. This is intended to provide an indication of the adviser's frequency of trading in those markets and the amount of liquidity hedge funds contribute to those markets. The proposal would have required the adviser to calculate a single turnover rate for its entire hedge fund portfolio. However, commenters warned that this would prove difficult to calculate if an adviser trades in many different instrument types and, in particular, that the value of certain types of derivatives would overwhelm the influence of other instruments on the aggregate turnover number.[243] These commenters suggested instead that we ask for turnover by asset class, as was done in the FSA Survey (and, more recently, ESMA's proposed reporting template).[244] We found these comments persuasive and have revised the question to request turnover in targeted asset classes.[245]

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242 *See* MSCI Letter (arguing that duration information may not be valuable for making comparisons across the industry because there are many ways in which it may be calculated).

243 *See* ABA Committees Letter; MFA Letter. Some commenters also argued that this question would not provide information valuable to monitoring systemic risk. *See*, *e.g.*, ABA Committees Letter; Fidelity Letter; SIFMA Letter. However, based on our consultation with staff representing FSOC's members, we believe that turnover will provide important insight into the role of hedge funds in providing trading liquidity in certain markets.

244 *See* FSA Survey, *supra* note 32; ESMA Proposal, *supra* note 33.

245 This is generally consistent with the international standards, though, unlike the FSA Survey and ESMA's proposed reporting template, we do not include derivatives (other

Question 27 has also been revised to request turnover data expressed as the value of transactions during the period rather than as a rate. This change has been made in order to make the data easier to compare to broader market data and to improve the comparability of the data with data that is or would be collected on the FSA survey and ESMA's proposed reporting template. In addition, we believe that the revised approach will be less burdensome for advisers than calculating the proposed portfolio turnover rate because advisers would have been required to determine the value of purchases and sales during the period as an intermediate step in calculating the portfolio turnover rate.[246]

Finally, in response to Question 28, the adviser must report a geographical breakdown of investments held by the hedge funds it advises.[247] This question has been modified from the proposal to require a less detailed breakdown (focusing on regions rather than countries) with additional, separate disclosure regarding investment in particular countries of interest. These changes are intended to respond to comments we received suggesting that advisers do not track this information in a manner consistent with our proposed, more granular geographical breakdown.[248] We anticipate that the

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than futures) because we have focused on assets classes where we believe turnover is currently most likely to occur at rates that raise systemic concerns.

246 *See* the Proposing Release, *supra* note 12, for the proposed definition of "turnover rate" in the Glossary of Terms to Form PF.

247 *See* Question 28 on Form PF.

248 *See* ABA Committees Letter; MFA Letter. We have not, as one commenter suggested, used any particular service provider's methodology of categorizing geographical exposures because our staff understands, based on conversations with industry representatives, that there is no single methodology that hedge fund advisers employ. *See* MFA Letter (suggesting that we use "Bloomberg's country of risk methodology"). In response to commenter concerns, we have removed some of the instructions regarding how the location of investments should be determined and expanded Instruction 15 to explain that the numerator should be calculated in the same manner as gross asset value.

revised approach will reduce the burden of responding to this question because the less granular categories should allow more advisers to rely on their existing classifications.

The information required in section 2a is designed to assist FSOC in monitoring asset classes in which hedge funds may be significant investors and trends in hedge funds' exposures. In particular, it is intended to allow FSOC to identify concentrations in particular asset classes (or in particular geographic regions) that are building or transitioning over time. It will also aid FSOC in examining large hedge fund advisers' role as a source of liquidity in different asset classes. In some cases, section 2a requires that the information be broken down into categories that are designed to facilitate use in the FRB's flow of funds report, a tool that is used for evaluating trends in and risks to the U.S. financial system.[249] This information also is designed to address requirements under section 204(b)(3) of the Advisers Act specifying certain mandatory contents for records and reports that must be maintained and filed by advisers to private funds. For example, it will provide information about the types of assets held and trading practices.

One commenter expressed concern that advisers do not collect or calculate the exposure or turnover information that section 2a requires on a monthly basis or track

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See MFA Letter. These changes allow advisers to rely on their internal methodologies and service provider reports in determining where to report investments and, by using gross asset value, rather than the more general value definition set out in Instruction 15, avoid the possibility that the reported value of certain derivative instruments would overwhelm the influence of other instruments. We have also added a "supranational" region, which is intended to capture investments that, because of their multinational scope, cannot meaningfully be placed in a single region.

249 *See supra* note 218 and *infra* note 475. For example, in some cases the data is required to be broken down between issuers that are financial institutions and those that are not. The FRB publishes flow of funds data on a quarterly basis.

geographical concentrations.[250] As discussed above, we are adopting section 2a with several changes that are designed to address commenters' concerns and reduce the reporting burden, though we continue to believe that monthly exposure and turnover values will be important to allow FSOC to track trends in the industry and to discourage "window dressing."[251] We acknowledge that advisers may incur additional burdens in responding to these questions, and we have taken this into account in considering the costs and benefits of this rulemaking.[252] The revised approach to the information required in section 2a strikes an appropriate balance between the burden imposed and need for the information.

b. Section 2b of Form PF

Consistent with our proposal, section 2b of Form PF requires a large hedge fund adviser to report certain additional information about any hedge fund it advises that has a net asset value of at least $500 million as of the end of any month in the prior fiscal quarter (a "qualifying hedge fund").[253] Two commenters disagreed with limiting

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250 *See* ABA Committees Letter.

251 *See infra* notes 285-292 and accompanying text. *See also* Proposing Release, *supra* note 12, at text accompanying n. 120 for a discussion of potential uses for this data.

252 *See infra* sections IV.B and V of this Release (discussing increases in our burden and cost estimates in response to comments received).

253 *See* Instruction 3 to Form PF. An adviser is not required to complete section 2 with respect to a fund of hedge funds that satisfies the requirements described in Instruction 7 to Form PF. For purposes of determining whether a private fund is a qualifying hedge fund, the adviser must aggregate any parallel funds and funds that are part of the same master-feeder arrangement and, to the extent discussed above in section II.A.5 of this Release, any parallel managed accounts and relevant funds of related persons. *See* Instructions 5 and 6 to Form PF and the definition of "qualifying hedge fund" in the Glossary of Terms to Form PF. *See also infra* section II.C.5 of this Release for a discussion of parallel funds, master-feeder arrangements and aggregation for reporting

reporting on section 2b to hedge funds with net assets of $500 million or more, arguing that information regarding smaller funds is important to monitoring certain group behaviors relevant to systemic risk and that smaller funds are equally likely to engage in improper activities, such as insider trading.[254] Two other commenters argued for a higher threshold, suggesting that no fund of this size could be systemically important.[255] We are adopting the threshold as proposed because we believe it balances the needs of FSOC for information regarding relatively large hedge funds and the burdens of the more detailed reporting that section 2b requires.[256]

Also consistent with our proposal, Question 30 in section 2b requires reporting of the same information as that requested in section 2a regarding exposure to different types of assets except, in this case, the information is reported for each qualifying hedge fund, rather than on an aggregate basis. This question has been modified from the proposal in the same manner as Question 26.[257]

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purposes. This aggregation is intended to prevent an adviser from structuring its activities to avoid the reporting requirements.

254 *See* AFL-CIO Letter; AFR Letter.

255 *See* Fidelity Letter (arguing that the FSA threshold of $500 million, upon which the qualifying hedge fund threshold used in the Form PF is based, should be scaled to $2.4 billion based on the relative size of equity markets in the United States and the United Kingdom); SIFMA Letter. As discussed above, these comments appear to be based on the mistaken premise that the thresholds are intended to establish a cutoff separating the risky from the safe. To the contrary, the reporting thresholds are intended only to ensure that FSOC has sufficient context for its analysis while minimizing the burden imposed on advisers. We understand based on our staffs' consultation with staff representing FSOC's members that, in order to assess potential systemic risk posed by the activities of certain funds, FSOC would benefit from access to data about funds that, on an individual basis, may not be a source of systemic risk.

256 In addition, certain of the information that would be obtained with respect to smaller hedge funds will already have been captured on an aggregate basis in section 2a.

257 *See supra* notes 233-242 and accompanying text for a discussion of those changes.

Section 2b also requires, on a per fund basis, data not requested in section 2a. For instance, the adviser must report information regarding the qualifying hedge fund's portfolio liquidity,[258] holdings of unencumbered cash[259] and concentration of positions.[260] These questions have been modified from the proposal to allow advisers to rely more on their own methodologies in responding, consistent with our changes to Instruction 15 to the Form, and to align the Form more closely with ESMA's proposed

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258 *See* Question 32 on Form PF. This question requires reporting of the percentage of the fund's portfolio capable of being liquidated within different time periods. *See* Proposing Release, *supra* note 12, at text accompanying n. 124 for a discussion of potential uses for this data. We have modified the instructions to this question to address commenter concerns by allowing advisers to rely more on their own methodologies in responding. *See* CCMR Letter; MFA Letter. We have also conformed the liquidity periods to those included in ESMA's proposed reporting template. *See* ESMA Proposal, *supra* note 33. One commenter objected to the question more generally, saying that the data is not currently tracked in the manner required and many firms would need to "devote significant time and resources" to building models and systems. TCW Letter. Another commenter, however, supported this question, noting that "[t]his [information] is increasingly a request of hedge fund investors, particularly for comingled funds, where a given investor can be adversely impacted by a sudden large redemption by another party." MSCI Letter. We have taken into account both of these comments in considering the costs and benefits of this rulemaking and believe that the value of the information to FSOC warrants the potential burden imposed. *See infra* sections IV.B and V of this Release (discussing increases in our burden and cost estimates in response to comments received).

259 *See* Question 33 on Form PF. In response to a comment we received, we have modified the definition of "unencumbered cash" to include the value of "overnight repos" used for liquidity management (so long as the assets purchased are U.S. treasury securities or agency securities) because we are satisfied that, for this purpose, the liquidity of these positions is sufficiently cash-like. *See* MFA Letter.

260 *See* Questions 34 and 35 on Form PF. Question 34 requires the total number of open positions held by the fund, and Question 35 requires reporting, for each position that represents 5% or more of the fund's net asset value, of the position's portion of the fund's net asset value and sub-asset class. One commenter asked for clarification regarding the meaning of "position," as used in these questions and elsewhere in the Form. *See* MFA Letter. In response, we have added an instruction to the Form explaining that advisers should determine whether a set of legal and contractual rights constitutes a "position" in a manner consistent with their internal recordkeeping and risk management procedures. *See* Instruction 15 to Form PF. This general instruction also supplants the detailed instructions proposed in Question 35, which have, accordingly, been removed.

reporting template. A new Question 31 has been added, which requires the adviser to identify the reporting fund's base currency because this information is necessary to interpret responses to questions regarding foreign exchange exposures and the effect of changes in currency rates on the reporting fund's portfolio.[261]

In Questions 36 through 38, the adviser must also provide information regarding the fund's collateral practices with counterparties.[262] These questions have been significantly modified from the proposal in order to reduce the amount of detail required, including by removing the breakdown of collateral into initial and variation margin. These changes were made because a commenter persuaded us that "[w]hile some of this information is potentially illuminating in the context of systemic risk... this section [as proposed] is more burdensome than it need be for its purpose."[263] We have also modified these questions by requiring information regarding rehypothecation only with respect to the fund's aggregate collateral (rather than on a counterparty-by-counterparty basis). Commenters persuaded us that, because collateral is often fungible, this question would have been difficult to answer as proposed and that the additional detail is unnecessary.[264] We anticipate that these changes will reduce the burden of responding to these questions.

Question 39 in section 2b also requires the adviser to report whether the hedge fund cleared any trades directly through a central clearing counterparty ("CCP") during

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261 *See also* Question 30, regarding reporting fund exposures, and Question 42, regarding the effect of changes in certain market factors on the fund's portfolio.

262 Questions 36 and 37 focus on collateral practices with the fund's top five counterparties, and Question 38 focuses on rehypothecation of the fund's aggregate collateral.

263 MSCI Letter.

264 *See* MFA Letter; MSCI Letter.

the reporting period. The proposal would have required the adviser to identify the three CCPs to which the fund has the greatest net counterparty credit exposure and provide the amount of that exposure. The information this question requires has been significantly reduced because commenters argued persuasively that the fund's relationship is typically with a swap dealer, futures commission merchant or direct clearing member who then interacts with the CCP rather than directly with a CCP and that, as a result, advisers "may not have easy access to the data requested by this question."[265] If responses to the revised question indicate that many reporting funds clear transactions directly through CCPs, the Commissions may consider in the future whether a question like the one proposed should be added to the Form. The change to Question 39 will reduce the burden of responding to the Form.

The information that Questions 30 through 35 require is designed to assist FSOC in monitoring the composition of hedge fund exposures over time as well as the liquidity of those exposures. In addition, information reported in response to Questions 36 through 38 is intended to aid FSOC in its monitoring of credit counterparties' unsecured exposure to hedge funds as well as the hedge fund's exposure and ability to respond to market stresses. Finally, Question 39 is intended to assist FSOC in monitoring whether hedge funds and CCPs become increasingly interconnected over time. This information could be important to understanding, for instance, concentrations in the hedge fund industry and interconnectedness, which relate to the factors that FSOC must consider in

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[265] MFA Letter; *see also* AIMA General Letter.

making a determination to designate a nonbank financial company for FRB supervision under the Dodd-Frank Act.[266]

Section 2b also requires for each qualifying hedge fund data regarding certain hedge fund risk metrics. For instance, Question 40 requires the adviser to report value at risk ("VaR") for each month of the reporting period if, during the reporting period, the adviser regularly calculated a VaR metric for the qualifying hedge fund. One commenter confirmed that, "[f]or all but the most illiquid strategies, hedge fund managers utilize these statistical measures [VaR and similar measures] for internal management and for investor reporting."[267] We are adopting this question substantially as proposed but with several clarifying changes.[268]

In Question 41, the adviser must also indicate whether there are risk metrics other than, or in addition to, VaR that it considers important to managing the fund's risks. Several commenters, noting that some advisers do not use VaR, expressed concern that a negative response regarding the use of VaR would create a presumption that the adviser

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266 *See* section 113(a) of the Dodd-Frank Act; FSOC Second Notice, *supra* note 6.

267 *See* MSCI Letter. This commenter, however, cautioned that variability in the calculation of VaR will make meaningful aggregation of this information difficult and suggested removing the question. As proposed, in order to minimize the reporting burden associated with this question, we are not requiring that all advisers calculate VaR using a standardized set of assumptions. Although this approach may, as the commenter suggested, reduce the ability of regulators to make comparisons across hedge funds using this data, we believe that it will also provide valuable risk information with respect to individual funds.

268 For instance, we have specified the units for reporting the confidence interval and weighting factor, combined the "none" and "equal" weighting options and clarified that the monthly reporting should be at the end of each month and not for the span of the month.

is not prudently managing risk.[269] This new question will give advisers an opportunity to indicate that they are using risk metrics other than VaR, and it will also provide valuable information regarding industry practice that may inform FSOC's understanding of risk management and future rulemakings.

In addition, Question 42 requires the adviser to report the impact on the fund's portfolio from specified changes to certain identified market factors, if regularly considered in formal testing in the fund's risk management, broken down by the long and short components of the qualifying hedge fund's portfolio. We are adopting this question with several changes from the proposal.[270] Most of the changes clarify the instructions, but the question has also been modified so that an adviser may omit a response to any market factor that it did not regularly consider in formal testing even if the factor could have an impact on the fund's portfolio or the adviser considered it qualitatively.[271] Under the proposal, an adviser would have been permitted to omit a response with respect to a market factor only if it did not regularly consider that factor in the reporting fund's risk management, whether in formal testing or otherwise. This change has been made in response to commenter concerns regarding the potential burden of responding to this

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269 *See* IAA Letter; MFA Letter.

270 These include changes intended to clarify (1) how the fund's portfolio should be separated into long and short components, (2) the period over which the changes should be deemed to occur and (3) how to address factors that would otherwise become negative when a given change is applied. We have also modified the magnitude of some of the market factor changes that advisers must test in order to reflect recent data on the frequency with which such changes may occur.

271 For this purpose, "formal testing" means that the adviser has models or other systems capable of simulating the effect of a market factor on the fund's portfolio, not that the specific assumptions outlined in the question were used in testing. If the factor is relevant but not tested, the adviser would need to check a box to that effect but would not report a numerical response.

question.[272] We believe it will reduce that burden in the aggregate because fewer advisers will need to provide detailed responses and for individual advisers because those without existing quantitative models will not be required to build or acquire them in order to respond to the question.

Some commenters would have preferred removal of Question 42 entirely, arguing that it would not yield information valuable to systemic risk monitoring because the variability in responses would hinder the ability of regulators to make comparisons across funds.[273] However, although variability in the assumptions used to complete the question may limit certain types of industry-wide comparisons, the variability itself, when taken together with other information collected on the Form, may provide important comparative information. Based on our staffs' consultations with staff representing

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272 *See, e.g.*, TCW Letter. This commenter wrote that "[a]n analyst at the firm estimated that it would take one to two days for the firm's systems to compute and verify the data for one fund's response to [this question]." Based on a discussion with this commenter, our staff understands that this estimate assumes that the fund holds securities that are very complex to model (such as non-agency mortgage backed securities) and that the modeling is intended to achieve a high level of confidence. Our staff further understands that for many other asset classes, this modeling would require minutes or hours rather than days and that, even for complex securities, advisers are able to obtain approximations about which they are reasonably confident in significantly less time. As a result, we believe that this commenter's estimate represents an effort significantly beyond the likely *average* burden this question requires. We also understand that the majority of the estimated one to two days represents time spent allowing the adviser's systems to calculate the responses and not employee hours. We note, finally, that we have significantly extended the filing deadline for large hedge fund advisers, reducing the likelihood that this task will compete with other tasks for the firm's computing resources and, consequently, the potential systems costs associated with this question. *See supra* section II.B.2 of this Release. Nonetheless, we have taken this comment into account in considering the costs and benefits of this rulemaking. *See infra* sections IV.B and V of this Release (discussing increases in our burden and cost estimates in response to comments received).

273 *See* IAA Letter; TCW Letter.

FSOC's members, we believe this question will also provide valuable risk information with respect to individual funds.[274]

Item D of section 2b also requires reporting of certain financing information for each qualifying hedge fund in Question 43. This question includes a monthly breakdown of the fund's secured and unsecured borrowing, the value of the collateral and other credit support posted in respect of the secured borrowing and the types of creditors. Question 43 has been modified from the proposal to clarify instructions and remove some of the detail regarding collateral postings (including information regarding rehypothecation of collateral, which is now covered on an aggregate basis elsewhere in section 2b).[275] We anticipate that these changes will reduce the burden of responding to this question. One commenter argued that advisers would have difficulty responding to the parts of Question 43 relating to the fund's borrowings via prime brokerage because they lack transparency into the prime brokerage relationship.[276] This comment suggests, however, that prime brokers do not currently report this information to advisers, not that advisers are unable to obtain this information on request. It should be noted that advisers have successfully completed the FSA Survey, which includes a similar breakdown of

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274 *See* Proposing Release, *supra* note 12, at text accompanying n. 127 (discussing potential uses for this data). One commenter suggested removing this question in favor of expanding the questions regarding counterparty exposures so that an adviser would complete those questions using multiple stress scenarios to probe for contingent exposures. *See* MSCI Letter; *see also supra* note 230. We believe at this time that the question we are adopting strikes a more appropriate balance between the value of the information collected and the burden of reporting.

275 *See supra* note 264 and accompanying text.

276 *See* MFA Letter.

borrowings (though not the collateral information), and that the revisions we have made to this question simplify the collateral reporting requirements.

An adviser must also report in Questions 44 and 45 the fund's total notional derivatives exposures as well as the net mark-to-market value of its uncleared derivatives positions and the value of the collateral and other credit support posted in respect of those uncleared positions. Under the proposal, advisers would have reported only the notional value of the fund's derivatives positions and the value of collateral posted in respect of those positions. One commenter pointed out, however, that the "absolute value of notional values cannot meaningfully be compared to variation margin amounts" because margin is posted based on net market values rather than notional amounts.[277] At this commenter's suggestion, this question has been revised to request both notional value and net market value. We have, however, narrowed the scope of transactions about which collateral information is requested. Specifically, an adviser is required to report market values and collateral values only for transactions that are not cleared by a CCP. We have taken this approach because we believe margining practices associated with cleared derivatives make obtaining information regarding collateral practices in connection with those transactions unnecessary. For the same reasons discussed above in connection with changes made to Questions 36 and 37, this question has been revised to reduce the amount of detail required regarding the posting of collateral.[278] We anticipate that these changes will, on net, reduce the burden of responding to Questions 44 and 45

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277 *See* MFA Letter.

278 *See supra* notes 262-264 and accompanying text.

and, by allowing comparisons of collateral practices to net exposures, provide more valuable information for FSOC.

In response to Questions 46 and 47, the adviser must provide a breakdown of the term of the fund's available financing and the identity of, and amount owed to, each creditor to which the fund owed an amount equal to or greater than 5 percent of the fund's net asset value as of the reporting date.[279] One commenter argued that the breakdown of available financing should not include uncommitted lines of credit because the lender may not provide them on request.[280] However, the extent to which financing may become rapidly unavailable is precisely the information this question is designed to elicit. We are adopting Questions 46 and 47 substantially in the form proposed.[281]

The information that Item D of section 2b requires is designed to assist FSOC in monitoring, among other things, the qualifying hedge fund's leverage, the unsecured exposure of credit counterparties to the fund, and the committed term of that leverage, which may be important to monitor if the fund comes under stress. This information is also relevant to the fund's interconnectedness and leverage, which relate to factors that FSOC must consider in making a determination to designate a nonbank financial company for FRB supervision under the Dodd-Frank Act.[282]

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279 To improve international consistency, we have conformed the liquidity periods in Question 46 to those included in ESMA's proposed reporting template. *See* ESMA Proposal, *supra* note 33. As explained above, we have moved Question 47 from section 1b to section 2b. *See supra* note 195.

280 *See* MFA Letter.

281 *But see, supra* note 279. We have also added an instruction to Question 47 clarifying that the precise legal name of the creditor is not required.

282 *See* section 113(a) of the Dodd-Frank Act; FSOC Second Notice, *supra* note 6.

Item E of section 2b requires the adviser to report information about each qualifying hedge fund's investor composition and liquidity. Questions 48 and 49, for example, require information regarding the fund's side-pocket and gating arrangements. These questions have been modified to increase their clarity and to require numerical responses regarding gating arrangements only if investors have withdrawal or redemption rights in the ordinary course, potentially reducing the number of advisers that need to respond to all elements of Question 49. Question 48 has also been expanded so that the adviser must check a box indicating whether additional assets have been placed in a side-pocket since the end of the prior reporting period. Without this additional information, FSOC would not be able to distinguish between advisers frequently using side-pockets and those who have simply had a side-pocket in place for an extended period. We believe, therefore, that this additional information will be important to interpreting the information proposed to be collected. We do not anticipate that this addition will significantly increase the burden of responding to this question because we believe that advisers already track assets held in side-pockets and the response only requires checking a box.

Finally, the adviser must provide, in Question 50, a breakdown of the percentage of the fund's net asset value that is locked in for different periods of time. This question has been modified from the proposal to clarify instructions and to improve international consistency by conforming the liquidity periods to those included in ESMA's proposed reporting template.[283]

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283 *See* ESMA Proposal, *supra* note 33.

The information that Item E of section 2b requires is designed to allow FSOC to monitor the hedge fund's susceptibility to failure through investor redemptions in the event the fund experiences stress due to market or other factors. For instance, this information, together with information collected in Questions 32 and 46 and elsewhere on the Form, is intended to assist FSOC in determining whether the fund may have a mismatch in the maturity or liquidity of its assets and liabilities, which relate to factors that FSOC must consider in making a determination to designate a nonbank financial company for FRB supervision under the Dodd-Frank Act.[284]

Certain data in the Form, while filed with the Commissions on an annual or quarterly basis, must be reported on a monthly basis to provide sufficiently granular data to allow FSOC to better identify trends and to mitigate "window dressing."[285] Nearly all of these requirements appear in section 2 of the Form, which only large hedge fund advisers complete. Although no commenters expressly supported the monthly data requirements within the Form, some commenters recommended that large advisers be required to file more often than quarterly, which could impose a greater burden than monthly reporting on a quarterly filing.[286] Several commenters, however, suggested that advisers should only report data as of the end of the quarterly reporting period.[287] One commenter, while conceding that some funds already report certain data to investors on a

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284 *See* section 113(a) of the Dodd-Frank Act; FSOC Second Notice, *supra* note 6.

285 *See*, *e.g.*, Questions 27, 28, 31, 33, 34, 43, 44, 45 and 56 on Form PF.

286 *See* AFL-CIO Letter; AFR Letter. *See also* CII Letter.

287 *See*, *e.g.*, BlackRock Letter (arguing that data should be provided, at most, on a quarterly basis); Fidelity Letter; MFA Letter; SIFMA Letter (proposing that reporting be no more frequent than quarterly, at least for private equity fund advisers).

monthly basis, asserted that such monthly reporting involves significantly less data and is based on internal valuation estimates only.[288] Other commenters doubted that advisers would engage in "window dressing" and argued that the increased costs to advisers would outweigh the benefits.[289]

Based on our staffs' consultations with staff representing FSOC's members, we agree with commenters who argued that rapidly changing markets and portfolios merit collecting certain information more often than on a quarterly basis, and we are not persuaded that the large hedge fund and large liquidity fund advisers required to respond to these questions will be overwhelmed by this reporting. Also, as discussed above, we have made several changes that increase the ability of advisers to rely on their own internal methodologies in responding to the Form, which is expected to ease the burden of reporting monthly information by clarifying that advisers need not incur substantial additional burdens in verifying the data.[290] Finally, the monthly data about which commenters were most concerned were the monthly performance data proposed to be collected in section 1b of the Form.[291] Question 17 has, however, been modified to require monthly data only in the case that the adviser is already calculating it, making the reporting burden essentially one of copying information onto the Form.[292] Accordingly,

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288 *See* BlackRock Letter.

289 *See, e.g.*, Fidelity Letter; MFA Letter.

290 *See supra* note 188 and text accompanying.

291 *See* Question 17 on Form PF; *supra* section II.C.1.b of this Release.

292 *See supra* nn. 198-202 and accompanying text.

except as discussed above, we are adopting the requirements to report monthly information as proposed.

3. Section 3 of Form PF

A private fund adviser must complete section 3 of Form PF if it manages one or more liquidity funds and had at least $1 billion in combined liquidity fund and registered money market fund assets under management as of the end of any month in the prior fiscal quarter.[293] Section 3 requires that the adviser report certain information for each liquidity fund it manages. The adviser must provide information regarding the fund's portfolio valuation and its valuation methodology, as well as the liquidity of the fund's holdings.[294] This section also requires information regarding whether the fund, as a matter of policy, is managed in compliance with certain provisions of rule 2a-7 under the Investment Company Act, which is the principal rule through which the SEC regulates registered money market funds.[295] Items B and C of section 3 require the adviser to report the amount of the fund's assets invested in different types of instruments,

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293 *See* sections II.A.2 and II.B.4 of this Release for the definition of "liquidity fund" and a discussion of this reporting threshold. *See also* Instructions 3, 5 and 6 to Form PF. Form PF is a joint form between the SEC and the CFTC only with respect to sections 1 and 2 of the form. Section 3 of the form, which requires more specific reporting regarding liquidity funds, is only required by the SEC.

294 *See* Questions 52, 53 and 55 on Form PF. The SEC has modified the instructions to Question 55 to clarify the units in which responses are to be reported and to clarify that the net asset value requested in parts (a) and (b) of Question 55 is the net asset value reported to current and prospective investors, which may or may not be the same as the net asset value reported in Questions 9 and 55(c), which are based on fair value.

295 *See* Question 54 of Form PF. The restrictions in rule 2a-7 are designed to ensure, among other things, that money market funds' investing remains consistent with the objective of maintaining a stable net asset value. Many liquidity funds state in investor offering documents that the fund is managed in compliance with Investment Company Act rule 2a-7 even though that rule does not apply to liquidity funds.

information for each open position of the fund that represents 5 percent or more of the fund's net asset value and information regarding the fund's borrowings.[296] Finally, Item D of section 3 asks for certain information regarding the fund's investors, including the concentration of the fund's investor base and the liquidity of its ownership interests.[297]

The information that section 3 requires is designed to assist FSOC in assessing the risks undertaken by liquidity funds, their susceptibility to runs, and how their investments might pose systemic risks either among liquidity funds or through contagion to registered money market funds. In addition, this information is intended to aid FSOC in monitoring leverage practices among liquidity funds and their interconnectedness to securities lending programs, which relate to factors that FSOC must consider in making a determination to designate a nonbank financial company for FRB supervision under the Dodd-Frank Act.[298] Finally, this information will assist FSOC in assessing the extent to which the liquidity fund is being managed consistent with restrictions imposed on registered money market funds that might mitigate their likelihood of posing systemic

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296 *See* Questions 56-59 on Form PF. The SEC has modified these questions from the proposal by removing instructions that have been supplanted by general instructions. *See* Instruction 15 to Form PF.

297 *See* Questions 60-64 on Form PF. For purposes of these questions, beneficial owners are persons who would be counted as beneficial owners under section 3(c)(1) of the Investment Company Act or who would be included in determining whether the owners of the fund are qualified purchasers under section 3(c)(7) of that Act. (15 U.S.C. 80a-3(c)(1) or (7)). The SEC has made clarifying changes to the instructions to Question 64. To improve international consistency, the SEC has also conformed the liquidity periods in Question 64 to those included in ESMA's proposed reporting template. *See* ESMA Proposal, *supra* note 33.

298 *See* section 113(a) of the Dodd-Frank Act; FSOC Second Notice, *supra* note 6.

risk. Commenters generally did not address the requirements of section 3, and the SEC is, therefore, adopting this section of the Form substantially as proposed.[299]

4. Section 4 of Form PF

A private fund adviser must complete section 4 of Form PF if it had at least $2 billion in private equity fund assets under management as of the end of its most recently completed fiscal year.[300] This section of the Form requires additional information regarding the private equity funds these advisers manage, which has been tailored to focus on relevant areas of financial activity that have the potential to raise systemic concerns. As discussed in the Proposing Release, information regarding the activities of private equity funds, certain of their portfolio companies and the creditors involved in financing private equity transactions may be important to the assessment of systemic risk.[301] The Proposing Release identified two practices of private equity funds, in particular, that could result in systemic risk: (1) the potential shift of market risk to lending institutions when bridge loans cannot be syndicated or refinanced;[302] and (2) the

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299 The SEC received only one comment specifically addressing the requirements of section 3, which questioned whether requiring information regarding investor liquidity is appropriate considering the focus of liquidity funds on short-term investments. *See* MFA Letter. The SEC continues to believe that this information is important to understanding whether a fund may suffer a mismatch between the maturity of its obligations and the maturity of its investments and is, therefore, adopting this question substantially as proposed. *But see*, *supra* note 297.

300 *See* Instruction 3 to Form PF. *See also* sections II.A.3 and II.B.4 of this Release for the definition of "private equity fund" and a discussion of this reporting threshold. Form PF is a joint form between the SEC and the CFTC only with respect to sections 1 and 2 of the form. Section 4 of the form, which requires more specific reporting regarding private equity funds, is only required by the SEC.

301 *See* Proposing Release, *supra* note 12, at section II.A.3.

302 *See* Proposing Release, *supra* note 12, at nn. 71-73 and accompanying text.

imposition of substantial leverage on portfolio companies that may themselves be systemically significant.[303]

Several commenters agreed that the activities identified in the Proposing Release are important areas of concern for monitoring systemic risk with respect to private equity funds.[304] Other commenters, however, disagreed with the analysis, arguing that private equity funds and their advisers do not have the potential to pose systemic risk.[305] These commenters affirmed that certain characteristics identified in the Proposing Release, including limitations on investor redemption rights and an absence of significant leverage at the fund level, are common to private equity funds and tend to mitigate their potential for systemic risk.[306]

The SEC acknowledges that several potentially mitigating factors suggest that private equity funds may have less potential to pose systemic risk than some other types of private funds, and this has been taken into account in requiring substantially less

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303 *See* Proposing Release, *supra* note 12, at nn. 74-75 and accompanying text.

304 *See, e.g.*, AFL-CIO Letter (pointing to evidence that the use of so-called "covenant-lite" loans is again expanding); CPIC Letter (noting the importance of gathering information about all types of entities using leverage and asserting that, "the Commission should not be pressured to scale back further or provide broad exemptions for private equity funds."); Merkl February Letter. *See also* Proposing Release, *supra* note 12, at n. 73 and accompanying text (discussing risks associated with "covenant-lite" loans).

305 *See, e.g.*, Olympus Letter; PEGCC Letter (contending that private equity funds are like any other shareholders and that they should not be singled out for "a discriminatory and onerous reporting regime designed to monitor how their portfolio companies use leverage."); SIFMA Letter.

306 *See, e.g.*, Olympus Letter; PEGCC Letter; SIFMA Letter. These commenters also noted that these funds typically focus on long-term investments and are legally isolated from the financial obligations of portfolio companies and other funds. They also asserted that private equity funds and their investments tend to be relatively small and are not interconnected. *See also* Proposing Release, *supra* note 12, at n. 77 and accompanying text.

information with respect to private equity funds than with respect to hedge funds or liquidity funds. The design of Form PF, however, is not intended to reflect a determination as to where systemic risk exists but rather to provide empirical data to FSOC with which it may make a determination about the extent to which the activities of private equity funds or their advisers pose such risk.[307] Based on SEC staff's consultation with staff representing FSOC's members, the SEC continues to believe that targeted information regarding private equity leverage practices may be important to FSOC's monitoring of systemic risk.[308]

One commenter argued that, if the SEC is concerned only with the use of leverage, the information could be gathered more effectively from the financial institutions that lend the money or, in the case of leveraged portfolio companies that are themselves financial institutions, incur the debt.[309] Staff representing FSOC's members has explained to the SEC's staff, however, that collecting leverage data from private

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307 One industry observer has explained the importance of transparency in allowing regulators to examine where risks may exist in the alternative investment industry, arguing that, "[r]egulation has to aim at trying to prevent the next crisis, not simply cleaning up the mess from the previous one. It may indeed be the case that the alternative investment industry is too small and/or is leveraged at too low a level, at least relative to average bank sector leverage, to be a likely source of future systemic harm but the opacity issue, which has for a long time hampered supervisors' efforts to understand the industry's significance, makes this hard to tell. Requiring the industry to submit at least to disclosure and transparency obligations that help regulators and central banks do a better job of identifying systemic risk concentrations in the system is a reasonable step forward. Resistance to the imposition of obligations of this sort would merely serve to suggest that there is something to hide." Eilis Ferran, *The Regulation of Hedge Funds and Private Equity: A Case Study in the Development of the EU's Regulatory Response to the Financial Crisis*, University of Cambridge and European Corporate Governance Institute (Feb. 2011).

308 *See* Proposing Release, *supra* note 12, at section II.A.3.

309 *See* PEGCC Letter.

equity advisers has several potential advantages. First, it provides a more complete accounting than other data sources of the leverage that may have been imposed on portfolio companies. Although portfolio companies may take on leverage through financial institutions regulated in the United States, they may also incur leverage from other sources, including hedge funds and foreign financial institutions. As a result, portfolio company leverage information collected through U.S. bank regulators would likely provide an incomplete picture and may fail to capture trends with potential systemic importance, such as greater reliance on leverage obtained from outside the regulated financial sectors or from foreign sources. Even if regulators are only concerned about the risks that a portfolio company's debt may impose on financial institutions, those risks cannot be fully understood without information regarding the company's entire balance sheet, including debt from other sources.

Second, because the SEC understands that private equity advisers routinely track the leverage of their portfolio companies, collecting data directly from these advisers is likely to be the most efficient means of monitoring portfolio company leverage. In contrast, obtaining portfolio company leverage information through bank regulators could be less efficient because (1) banks are less likely to be actively tracking leverage information specifically attributable to portfolio companies, (2) bank regulators do not have a single collection mechanism for this data and (3) data may need to be aggregated across several different bank regulators.

Third, collecting leverage data from private equity advisers would fill gaps in the data that could appear if FSOC were to attempt aggregating information from many different U.S. bank regulators. It also provides a check on any data that may be collected

from other sources. Indeed, other types of information that the SEC collects from investment advisers has already proven valuable in cross-checking data that bank regulators collect.[310]

Fourth, FSOC has stated that it is concerned that leveraged lending practices can raise systemic risk concerns.[311] Private equity advisers are repeat participants in the leveraged loan market (often more so than other types of companies that access credit through these markets), and tracking their portfolio company leverage practices can signal trends in emerging risks in those markets. Indeed a recent study found that the private equity fund sponsors' bank relationships were an important factor in explaining the favorable loan terms obtained by private equity portfolio companies, both as a result of the private equity sponsor's repeat interactions reducing information asymmetries and the competition among banks to cross-sell other business to the private equity sponsor.[312] This empirical data suggests that collecting data on private equity portfolio company leverage trends in fact may be the most efficient way to collect systemic risk trend data for the broader leveraged loan market because private equity portfolio companies' practices in this area may be a bellwether due to their sponsors' repeat player status. In

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310 The SEC's Form N-MFP, for instance, has provided a valuable check against information that banking regulators collect with respect to portfolio holdings of registered money market funds.

311 *See* FSOC 2011 Annual Report, supra note 19, at 12 ("Although it is difficult to make definitive determinations regarding the appropriateness of risk pricing, there have been some indicators that credit underwriting standards might have overly eased in certain products, such as leveraged loans, reflecting the dynamics of competition among arranging bankers. …Sound underwriting standards, which were abandoned in the run-up to the crisis, will encourage greater investor confidence and stability in the market")

312 *See* Victoria Ivashina & Anna Kovner, *The Private Equity Advantage: Leveraged Buyout Firms and Relationship Banking*, 24 REV. OF FIN. STUDIES 7 (July 2011).

addition, this approach appears consistent with an emerging international approach favoring broad monitoring of credit intermediation across the economy.[313]

The SEC is, however, adopting Form PF with several significant changes that reduce the frequency of reporting with respect to private equity funds, as discussed above, and more closely align the required reporting with information available on portfolio company financial statements. These changes, which are discussed in detail below and in section II.B of this Release, are intended to respond to industry concerns while still providing FSOC the information it needs to monitor the potential for systemic risk across the private fund industry. In general, we expect that these changes will reduce the burden of responding to the Form.

Section 4 requires that large private equity advisers report certain information for each private equity fund they manage, including certain information about guarantees of portfolio company obligations and the leverage of the portfolio companies that the fund controls. Specifically, Question 66 requires information about the amount of guarantees that the adviser, the reporting fund or any other related person of the adviser issues in respect of a portfolio company's obligations.[314] Questions 67 through 70 require the

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313 *See* FSB Shadow Banking Report, *supra* note 28; ESMA Proposal, *supra* note 33; Proposing Release, *supra* note 12, at n. 33. *See also* CPIC Letter (affirming the importance of gathering information about all types of entities using leverage).

314 Following consultation with staff representing FSOC's members, we have broadened the scope of this question to capture guarantees from the adviser and its related persons rather than just those from the reporting fund. This change is intended to allow FSOC and other regulators to confirm broadly whether the adviser or the reporting fund has direct or indirect exposure to the liabilities of portfolio companies in excess of the amounts of their investments. In addition to Question 66, the proposal included a separate question regarding the fund's borrowings, but a commenter pointed out that this substantially duplicated the information requested in Question 13 on Form PF, so the proposed question is not being adopted. *See* comment letter of George Merkl (Mar. 23, 2011). *See*

adviser to report: (1) the weighted average debt-to-equity ratio of controlled portfolio companies in which the fund invests, (2) the range of that debt-to-equity ratio among these portfolio companies and (3) the aggregate gross asset value of these portfolio companies.[315]

In addition, Questions 71 and 72 ask for the total amount of borrowings categorized as current liabilities and as long-term liabilities on the most recent balance sheets of the fund's controlled portfolio companies. These questions replace the question that the SEC proposed, which would have required advisers to report the maturity profile of the debt of its private equity funds' controlled portfolio companies.[316] This change has been made in response to commenter concerns regarding the burden of gathering the data

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also the Proposing Release, *supra* note 12, for the proposed version of Question 57 on Form PF.

315 A "controlled portfolio company" is defined as a portfolio company that is controlled by the private equity fund, either alone or together with the private equity fund's affiliates or other persons that are, as of the reporting date, part of a club or consortium investing in the portfolio company. "Control" has the same meaning as used in Form ADV and generally means the power, directly or indirectly, to direct the management or policies of a person, whether through ownership of securities, by contract, or otherwise. *See* Glossary of Terms to Form PF; Glossary of Terms to Form ADV. One commenter suggested the average ratio required in Question 68 would be unreliable because it depends on accounting methodologies, which may vary. *See* PEGCC Letter. While this measure may have its limitations, the SEC believes, based on its staff's consultations with staff representing FSOC's members, that this question will provide an important indication of portfolio company leverage and is not aware of an alternative that would yield more reliable information without imposing additional burdens on advisers. Question 70, regarding the aggregate gross asset value of the reporting fund's controlled portfolio companies, has been added to provide a measure of scale as context for interpreting the average leverage ratio. An adviser must already know this information in order to calculate the average leverage ratio, so the SEC does not expect this addition to meaningfully increase the reporting burden.

316 *See* the Proposing Release, *supra* note 12, (discussing the proposed version of Question 62 on Form PF).

that would have been required to respond to the question as proposed.[317] The SEC anticipates that these changes will reduce the burden of responding to these questions because less information is required and the information will be readily available on the financial statements of the fund's controlled portfolio companies.

In response to Questions 73 and 74, the adviser must report the portion of the controlled portfolio companies' borrowings that is payment-in-kind or zero coupon,[318] and whether the fund or any of its controlled portfolio companies experienced an event of default on any of its debt during the reporting period.[319] In addition, Question 75 requires the adviser to provide the identity of the institutions providing bridge financing to the adviser's controlled portfolio companies and the amount of that financing. Question 76 requires certain information if the fund controls any financial industry portfolio company, such as the portfolio company's name, its debt-to-equity ratio, and the percentage of the portfolio company beneficially owned by the fund.[320] Question 79

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317 *See* IAA Letter.

318 *See* Question 73 on Form PF. One commenter argued that the SEC should not include this question because it has not identified any systemic risk associated with this type of indebtedness. *See* PEGCC Letter. The indebtedness in question, however, allows the borrower to increase its leverage by deferring interest payments (all at a time subsequent to the creditors making their credit determinations) and may result in additional risk being shifted to systemically important financial institutions or other holders of the debt.

319 *See* Question 74 on Form PF. One commenter suggested this question should cover only controlled portfolio companies rather than all of the fund's portfolio companies, and the SEC has made this change. *See* ABA Committees Letter; *see also infra* discussion accompanying notes 324-327. This commenter also suggested that potential events of default that have not ripened into events of default should not require an affirmative response, and the SEC has modified the instructions to this address this comment.

320 A "financial industry portfolio company" generally is defined as a nonbank financial company, as defined in the Dodd-Frank Act, or a bank, savings association, bank holding company, financial holding company, savings and loan holding company, credit union, or other similar company regulated by a federal, state or foreign banking regulator. *See*

requires the adviser to report whether any of its related persons co-invest in any of the fund's portfolio companies.

The information that Question 66 requires is intended to provide FSOC information regarding the exposure of large private equity advisers and their funds to the risks of their portfolio companies. The information that Questions 67 through 76 require is designed to allow FSOC to assess the potential exposure of banks and other lenders to the portfolio companies of funds managed by large private equity advisers and to monitor whether trends in those areas could have systemic implications. Information reported in response to Question 76 is also intended to allow FSOC to monitor investments by the funds of large private equity advisers in companies in the financial industry that may be particularly important to the stability of the financial system.

Finally, Questions 77 and 78 require a breakdown of the fund's investments by industry and by geography.[321] Two commenters suggested removing these questions, arguing that the value of the information would not exceed the burden of reporting it.[322] Regulators, however, will be able to use this information to monitor global and industry

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Glossary of Terms to Form PF. One commenter suggested this question should cover only controlled portfolio companies rather than all of the fund's portfolio companies, and the SEC has made this change. *See* ABA Committees Letter; *see also* IAA Letter; *see also infra* discussion accompanying notes 324-327. The SEC has added a requirement to report the gross asset value of each financial industry portfolio company to provide a measure of scale as context for interpreting the leverage ratio. This information should be readily available on portfolio company financial statements, so the SEC does not expect this addition to meaningfully increase the reporting burden.

321 The SEC has modified the instructions to these questions to reflect clarifications suggested by a commenter. *See* Merkl February Letter. Question 78, which requires a geographical breakdown of investments in portfolio companies, has also been modified for reasons discussed above. *See supra* note 247 and accompanying text.

322 *See* Merkl February Letter; PEGCC Letter.

concentrations among private equity funds, and concentration is one of the factors that FSOC must consider in making a determination to designate a nonbank financial company for FRB supervision under the Dodd-Frank Act.[323] In addition, the information required is largely based on the financial statements of the controlled portfolio companies and, therefore, should be readily available to the adviser.

Most of the reporting in section 4 relates to portfolio companies because the SEC understands that leverage in private equity structures is generally incurred at the portfolio company level. This reporting is limited to *controlled* portfolio companies, rather than portfolio companies generally, to ensure that advisers are able to obtain the relevant information without incurring potentially substantial additional burdens. Several commenters suggested, however, that the proposed standard of "control" was too low, leaving advisers responsible for reporting information they may not be entitled to access.[324] The SEC is not persuaded that advisers are likely to have such difficulty obtaining the information required concerning controlled portfolio companies because the majority of this information is available from the financial statements of the portfolio companies or relates to the fund's own investments in the portfolio companies.[325] In

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323 *See* section 113(a) of the Dodd-Frank Act.

324 *See, e.g.*, ABA Committees Letter (suggesting instead "a standard of majority voting control"); IAA Letter (asserting that an adviser may not have access to some of the required data "even if the fund owns 50% or more of such portfolio company"); PEGCC Letter. *See supra* note 315 (discussing the definition of "control.)"

325 Advisers may not know the North American Industry Classification System, or NAICS, codes for its controlled portfolio companies, but this information should be readily obtainable from the company. The details regarding bridge loans required in Question 75 on the Form may not be available directly from a controlled portfolio company's financial statements, but it is likely either that the adviser was involved in arranging or consenting to the loans (because the loans were an important part of the fund's

addition, modifications from the proposal have replaced a requirement for information that may not have been available on portfolio company financial statements with a requirement for information that will appear on any audited portfolio company's financial statements.[326] Accordingly, the SEC is adopting the definition of "controlled portfolio company" substantially as proposed.[327]

Two commenters supported collecting the information proposed to be required in section 4.[328] However, they also argued that the required reporting should not be restricted to controlled portfolio companies but should extend to all of the fund's portfolio companies. In their view, the largest portfolio companies are the least likely to have a controlling shareholder and the most likely to pose systemic risk. The SEC is sensitive to this concern but believes at this time that requesting information regarding all portfolio companies would increase the difficulty of responding to section 4 without a sufficiently large corresponding increase in the value of the data collected.

5. Aggregation of Master-Feeder Arrangements, Parallel Fund Structures and Parallel Managed Accounts

For purposes of reporting information on Form PF, an adviser may provide information regarding master-feeder arrangements and parallel fund structures in the

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investment in the company or because they were incurred after the fund obtained a controlling interest in the company) or were the subject of the fund's due diligence prior to investing in the company.

326 *See supra* note 317 and accompanying text.

327 The SEC has, however, made one change to this definition, which clarifies that whether a group is a club or consortium for this purpose should be determined as of the reporting date. In other words, the adviser need not aggregate the control rights of another fund with those of its own solely because, at some point prior to the reporting date, such as the date of acquisition, they formed a club or consortium.

328 *See* AFL-CIO Letter; AFR Letter.

aggregate or separately, provided that it does so consistently throughout the Form.[329] For example, an adviser may complete either a single section 1b for all of the funds in a master-feeder arrangement or a separate section 1b for each fund in the arrangement. Any adviser choosing to aggregate funds in the reporting must check the "yes" box in Question 6 or Question 7, as applicable, and, in the case of Question 7, provide the additional information required with respect to the other funds in the parallel fund structure.[330] Advisers are not required to report information regarding parallel managed accounts other than to complete Question 11 in section 1b of the Form.[331]

These aggregation requirements have been modified from the proposal, which would have required advisers to report aggregated information regarding master-feeder arrangements and parallel managed accounts but separate information regarding parallel funds. One commenter recommended that "the Commissions instead provide managers with flexibility to provide information about private funds in a manner that best represents the activities of their funds and is consistent with their internal reporting procedures, while providing complete information to regulators."[332] We are persuaded that requiring advisers to aggregate or disaggregate funds in a manner inconsistent with

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329 *See* Instructions 5 and 6 to Form PF. The aggregation requirements for reporting purposes differ from the aggregation requirements for determining whether the adviser or any fund meets a reporting threshold. *See supra* section II.A.5. A "parallel fund structure" is a structure in which one or more private funds pursues substantially the same investment objective and strategy and invests side by side in substantially the same positions as another private fund. *See* Glossary of Terms to Form PF. A "master-feeder arrangement" is an arrangement in which one or more funds ("feeder funds") invest all or substantially all of their assets in a single private fund ("master fund").

330 *See also supra* note 193 and accompanying text.

331 *See* Instructions 5 and 6 to Form PF. *See also supra* note 197.

332 MFA Letter.

their internal recordkeeping and reporting may impose additional burdens and that, so long as the structure of those arrangements is adequately disclosed, a prescriptive approach to aggregation is not necessary.

With respect to parallel managed accounts, commenters encouraged us not to require aggregation for reporting purposes or at least limit the questions that require advisers to aggregate parallel managed accounts for reporting purposes.[333] In particular, these commenters argued that aggregating these funds for reporting purposes would be difficult and "result in inconsistent and misleading data" because their characteristics are often somewhat different from the funds with which they are managed.[334] We are persuaded that including parallel managed accounts in the reporting may reduce the quality of data while imposing additional burdens on advisers. As a result, the instructions have been revised so that advisers are not required to aggregate parallel managed accounts with their private funds for reporting purposes.[335] A question has, however, been added to the Form requiring advisers to report the total amount of parallel managed accounts related to each reporting fund.[336] This will allow FSOC to take into account the greater amount of assets an adviser may be managing using a given strategy for purposes of analyzing the data reported on Form PF.

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333 *See, e.g.*, IAA Letter; TCW Letter. One commenter agreed that the proposal appropriately required reporting on parallel managed accounts. *See* AIMA General Letter. For the reasons discussed below, however, we are persuaded that the better approach is not to require aggregation of these accounts for reporting purposes.

334 IAA Letter. *See also* MFA Letter.

335 *See* Instructions 5 and 6 to Form PF. The approach we are adopting is also similar to the approach used in the FSA Survey, which asks for only limited information regarding "strategy assets." *See* IAA Letter.

336 *See* question 12 of Form PF.

D. Confidentiality of Form PF Data

Form PF elicits non-public information about private funds and their trading strategies, the public disclosure of which could adversely affect the funds and their investors. The SEC does not intend to make public Form PF information identifiable to any particular adviser or private fund, although the SEC may use Form PF information in an enforcement action. The Dodd-Frank Act amends the Advisers Act to preclude the SEC from being compelled to reveal this information except in very limited circumstances.[337] Similarly, the Dodd-Frank Act exempts the CFTC from being compelled under FOIA to disclose to the public any information collected through Form PF and requires that the CFTC maintain the confidentiality of that information consistent with the level of confidentiality established for the SEC in section 204(b) of the Advisers Act.[338] The Commissions will make information collected through Form PF available to FSOC, as the Dodd-Frank Act requires, subject to the confidentiality provisions of the Dodd-Frank Act.[339]

The Dodd-Frank Act contemplates that Form PF data may also be shared with other Federal departments or agencies or with self-regulatory organizations, in addition to the CFTC and FSOC, for purposes within the scope of their jurisdiction.[340] In each case, any such department, agency or self-regulatory organization would be exempt from being

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337 *See* Proposing Release, *supra* note 12, at n.39.

338 Form PF data is filed with the SEC, and made available to the CFTC, pursuant to section 204(b) of the Advisers Act, making this data subject to the confidentiality protections applicable to data required to be filed under that section.

339 *See* section 204(b) of the Advisers Act.

340 *See* section 204(b)(8)(B)(i) of the Advisers Act.

compelled under FOIA to disclose to the public any information collected through Form PF and must maintain the confidentiality of that information consistent with the level of confidentiality established for the SEC in section 204(b) of the Advisers Act.[341] Prior to sharing any Form PF data, the SEC also intends to require that any such department, agency or self-regulatory organization represent to us that it has in place controls designed to ensure the use and handling of Form PF data in a manner consistent with the protections established in the Dodd-Frank Act.[342]

Certain aspects of the Form PF reporting requirements also help to mitigate the potential risk of inadvertent or improper disclosure. For instance, because data on Form PF generally could not, on its own, be used to identify individual investment positions, the ability of a competitor to use Form PF data to replicate a trading strategy or trade against an adviser is limited.[343] In addition, the deadlines for filing Form PF have, in most cases, been significantly extended from the proposal.[344] Some commenters

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341 *See* sections 204(b)(9) and (10) of the Advisers Act.

342 This would be consistent with the SEC's current practice of requiring that it receive, prior to sharing nonpublic information with other regulators, "such assurances of confidentiality as the [SEC] deems appropriate." *See* section 24(c) of the Exchange Act and rule 24c-1 thereunder.

343 Questions 26, 30, 35 and 57 on Form PF ask about exposures of the reporting fund but require only that the adviser identify the exposure within broad asset classes, not the individual investment position. Large private equity advisers must identify any financial industry portfolio companies in which the reporting fund has a controlling interest, but these investments are likely to be in private companies whose securities are not widely traded (and, therefore, do not raise the same trading concerns) or in public companies about which information regarding significant beneficial owners is already made public under sections 13(d) and 13(g) of the Exchange Act.

344 *See supra* section II.B.2 of this Release (discussing filing deadlines).

supported these extensions in part because filings will, as a result, generally contain less current, and therefore less sensitive, data.[345]

In addition, our staff is working to design controls and systems for the use and handling of Form PF data in a manner that reflects the sensitivity of this data and is consistent with the confidentiality protections established in the Dodd-Frank Act. As discussed below, this will include programming the Form PF filing system with appropriate confidentiality protections.[346] For instance, SEC staff is studying whether multiple access levels can be established so that SEC employees are allowed only as much access as is reasonably needed in connection with their duties.

Several commenters confirmed that the information collected on Form PF is competitively sensitive or proprietary and emphasized the importance of controls for safekeeping.[347] These commenters also made several recommendations for protecting the data, including: (1) storing identifying information using a code;[348] (2) limiting the ability to transfer Form PF data by email or portable media;[349] (3) limiting access to personnel who "need to know";[350] (4) extending filing deadlines so the data contains less current information;[351] and (5) sharing the data with other regulators only in aggregated

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345 *See infra* note 351 and accompanying text.

346 *See infra* section II.E of this Release.

347 *See, e.g.*, ABA Committees Letter; AIMA General Letter; CPIC Letter; MFA Letter; SIFMA Letter.

348 ABA Committees Letter; Kleinberg General Letter; Seward Letter.

349 ABA Committees Letter.

350 *Id.*

351 AIMA General Letter; Kleinberg General Letter.

and anonymous form.[352] As discussed above, the deadlines for filing Form PF have, in most cases, been significantly extended from the proposal.[353] SEC staff is also carefully considering the other recommendations of commenters in designing controls and systems for Form PF.

In advance of the compliance date for Form PF, SEC staff will review the controls and systems in place for the use and handling of Form PF data.[354] Depending on the progress at that time toward the development and deployment of these controls and systems, the SEC will consider whether to delay the compliance date for Form PF.

E. Filing Fees and Format for Reporting

Under Advisers Act rule 204(b)-1(b), Form PF must be filed through an electronic system designated by the SEC for this purpose. On September 30, 2011, the SEC issued notice of its determination that the Financial Industry Regulatory Authority ("FINRA") will develop and maintain the filing system for Form PF as an extension of the existing Investment Adviser Registration Depository ("IARD").[355] This filing system will have certain features, including being programmed to reflect the heightened confidentiality protections created for Form PF filing information under the Dodd-Frank Act and allow for secure access by FSOC and other regulators as permitted under the Dodd-Frank Act.

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352 AIMA General Letter; Seward Letter.

353 *See supra* notes 344-345 and accompanying text.

354 *See infra* section III of this Release (discussing the compliance date for Form PF).

355 *See Approval of Filing Fees for Exempt Reporting Advisers and Private Fund Advisers*, Investment Advisers Act Release No. IA-3297 (Sept. 30, 2011), 76 FR 62100 (Oct. 6, 2011).

Under the Advisers Act rule 204(b)-1, advisers required to file Form PF must pay to the operator of the Form PF filing system fees that the SEC has approved.[356] The SEC in a separate order has approved filing fees that reflect the costs reasonably associated with these filings and the development and maintenance of the filing system.[357]

We are working with FINRA to allow advisers to file Form PF either through a fillable form on the system website or through a batch filing process utilizing the eXtensible Markup Language ("XML") tagged data format. In connection with the batch filing process, we anticipate publishing a taxonomy of XML data tags in advance of the compliance date for Form PF. We believe that certain advisers may prefer to report in XML format because it allows them to automate aspects of their reporting and thus minimize burdens and generate efficiencies for the adviser.

Commenters who addressed this aspect of the proposal supported having FINRA develop the reporting system as an extension of the IARD platform.[358] Commenters also supported a batch filing capability, with one specifically agreeing that "[a]utomated

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356 *See* Advisers Act rule 204(b)-1(d); section 204(c) of the Advisers Act.

357 *See Order Approving Filing Fees for Exempt Reporting Advisers and Private Fund Advisers*, Investment Advisers Act Release No. IA-3305 (Oct. 24, 2011).

358 *See* AIMA General Letter (agreeing that using the IARD and FINRA is a "sensible solution."); MFA Letter. We explained in the Form PF Proposing Release that the filing system would need to be programmed with special confidentiality protections designed to ensure the heightened confidentiality protections created for Form PF filing information under the Dodd-Frank Act. *See* Proposing Release, *supra* note 12, at n. 9 and accompanying text and section II.E. These commenters expressed the view that maintaining the confidentiality of Form PF data is an important consideration in developing the filing system. Our staffs are working closely with FINRA in designing controls and systems to ensure that Form PF data is handled and used in a manner consistent with the protections established in the Dodd-Frank Act, and as noted above, we are carefully considering recommendations from commenters in designing controls and systems for the use and handling of Form PF data.

submission of information via the IARD or other electronic system to [utilize] the eXtensible Markup Language (XML) tagged data format or similar format is likely to be an important time saver for a large number of firms."[359]

III. EFFECTIVE AND COMPLIANCE DATES

The effective date for CEA rule 4.27, Advisers Act rule 204(b)-1 and Form PF is March 31, 2012.

The Commissions are adopting a two-stage phase-in period for compliance with Form PF filing requirements. For the following advisers, the compliance date for CEA rule 4.27 and Advisers Act rule 204(b)-1 is June 15, 2012:

- Any adviser having at least $5 billion in assets under management attributable to hedge funds as of the last day of the fiscal quarter most recently completed prior to June 15, 2012; [360]
- Any adviser managing a liquidity fund and having at least $5 billion in combined assets under management attributable to liquidity funds and registered money market funds as of the last day of the fiscal quarter most recently completed prior to June 15, 2012;[361] and

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359 AIMA General Letter. *See also* Kleinberg General Letter.

360 For this purpose, advisers must calculate the value of assets under management pursuant to the instructions in Form ADV and aggregate assets under management in the same manner as they would when determining whether they satisfy reporting thresholds under Form PF. *See supra* section II.A.5 of this Release.

361 *Id.*

- Any adviser having at least $5 billion in assets under management attributable to private equity funds as of the last day of its first fiscal year to end on or after June 15, 2012.[362]

For instance, an adviser with $5 billion in hedge fund assets under management as of March 31, 2012, must file its first Form PF within 60 days following June 30, 2012.[363] In addition, an adviser having a June 30 fiscal year end and $5 billion in private equity fund assets under management as of June 30, 2012, must file its first Form PF within 120 days following June 30, 2012.[364]

For all other advisers, the compliance date for CEA rule 4.27 and Advisers Act rule 204(b)-1 is December 15, 2012. As a result, most advisers must file their first Form PF based on information as of December 31, 2012.

This timing provides most private fund advisers with a significant amount of time to prepare for filing, requiring only the largest advisers, whose resources and systems should better position them to begin reporting, to report in less than a year following adoption of Form PF. This approach is designed to balance the need for regulators to begin collecting and analyzing data regarding the private fund industry with the ability of advisers to efficiently prepare for filing. We currently anticipate that this timeframe will

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362 *Id.*

363 This assumes the adviser's fiscal quarters are based on calendar quarters. Of course, if the adviser also exceeds the threshold for liquidity fund advisers, its filing would be due within 15 days.

364 This assumes the adviser does not also exceed the $5 billion threshold for hedge fund or liquidity fund advisers.

also give the SEC sufficient time to create and program a system to accept filings of Form PF.[365]

We are adopting compliance dates that significantly extend the proposed compliance date of December 15, 2011. We are taking this approach, in part, because we are adopting these rules later than originally expected. The revised approach is also intended to respond to commenters who recommended a later compliance date. These commenters argued that the proposed compliance date would have provided advisers insufficient "time to identify the information to be included, establish automated systems and procedures to collect and calculate the information, and develop procedures to review, complete and verify the Form."[366] A majority of these commenters suggested extending compliance to at least nine months after publication of the final Form, though some argued for a year or more.[367] In support of an extended compliance date, commenters emphasized that, without sufficient time to prepare for the initial filing, the reporting process will be manually intensive or require costly system enhancements.[368] As explained above, our revised approach is designed to provide the largest advisers, whose resources and systems should better position them to begin reporting, at least eight

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365 The SEC is working closely with FINRA to create and program a system for Form PF filings, and FINRA expects to be able to accept Form PF filings in this timeframe.

366 MFA Letter. *See also infra* note 367.

367 *See, e.g.*, AIMA General Letter (nine months); BlackRock Letter (nine months); CPIC Letter (one year); Fidelity Letter (one year); IAA Letter (nine months); Kleinberg General Letter (one year); MFA Letter (nine months); PEGCC Letter (one year); TCW Letter (nine months); Seward Letter (two years); SIFMA Letter (nine months); USCC Letter (270 days).

368 *See* AIMA General Letter; Kleinberg General Letter.

months before they start filing Form PF, and the vast majority of advisers will have over a year before their first Form PF is due.

IV. PAPERWORK REDUCTION ACT

SEC:

Section 204(b) of the Advisers Act directs the SEC to require private fund advisers to file reports containing such information as the SEC deems necessary and appropriate in the public interest and for investor protection or for the assessment of systemic risk. Rule 204(b)-1 and Form PF under the Advisers Act implement this requirement. Form PF contains a new "collection of information" within the meaning of the Paperwork Reduction Act ("PRA").[369] The title for the new collection of information is: "Form PF under the Investment Advisers Act of 1940, reporting by investment advisers to private funds." For purposes of this PRA analysis, the paperwork burden associated with the requirements of rule 204(b)-1 is included in the collection of information burden associated with Form PF and thus does not entail a separate collection of information. The SEC is submitting this collection of information to the Office of Management and Budget ("OMB") for review in accordance with 44 U.S.C. 3507(d) and 5 CFR 1320.11. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid control number.

Form PF is intended to provide FSOC with information that will assist it in fulfilling its obligations under the Dodd-Frank Act relating to nonbank financial

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369 44 U.S.C. 3501-3521.

companies and systemic risk monitoring.[370] The SEC may also use the information in connection with its regulatory and examination programs. The respondents to Form PF are private fund advisers.[371] Compliance with Form PF is mandatory for any private fund adviser that had at least $150 million in regulatory assets under management attributable to private funds as of the end of its most recently completed fiscal year.

Specifically, smaller private fund advisers must report annually and provide only basic information regarding their operations and the private funds they advise. Large private equity advisers also must report on an annual basis but are required to provide additional information with respect to the private equity funds they manage. Finally, large hedge fund advisers and large liquidity fund advisers must report on a quarterly basis and provide more information than other private fund advisers.[372] The PRA analysis set forth below takes into account the difference in filing frequencies among different categories of private fund adviser. It also reflects the fact that the additional information Form PF requires large hedge fund advisers to report is more extensive than

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370 *See supra* section I.A of this Release; *see also* of the Proposing Release, *supra* note 12, at section II.A.

371 The requirement to file the Form applies to any investment adviser registered, or required to register, with the SEC that advises one or more private funds and had at least $150 million in regulatory assets under management attributable to private funds as of the end of its most recently completed fiscal year. *See* Advisers Act rule 204(b)-1(a). It does not apply to state-registered investment advisers or exempt reporting advisers.

372 *See* section II.A of this Release (describing who must file Form PF), section II.B of this Release (discussing the frequency with which private fund advisers must file Form PF), section II.C.2 of this Release (describing the information that large hedge fund advisers must report on Form PF), and sections II.C.3 and II.C.4 of this Release (describing the information that large liquidity and private equity fund advisers must report on Form PF). *See also* Instruction 9 to Form PF (discussing the frequency with which private fund advisers must file Form PF).

the additional information required from large liquidity fund advisers, which in turn is more extensive than that required from large private equity advisers.

As discussed in section II of this Release, the SEC has sought to minimize the reporting burden on private fund advisers to the extent appropriate. In particular, the SEC has taken into account an adviser's size and the types of private funds it manages in designing scaled reporting requirements. In addition, where practical, the SEC has permitted advisers to rely on their existing practices and methodologies to report information on Form PF.[373]

Advisers must file Form PF through the Form PF filing system on the IARD.[374] Responses to the information collections will be kept confidential to the extent permitted by law.[375]

A. Burden Estimates for Annual Reporting by Smaller Private Fund Advisers

In the Implementing Adopting Release, the SEC estimated that there will be approximately 4,270 SEC-registered advisers managing private funds after taking into account recent changes to the Advisers Act and a year of normal growth in the population of registered advisers.[376] The SEC estimates that approximately 700 of these advisers

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373 The SEC also believes that private fund advisers already collect or calculate some of the information required on the Form at least as often as they must file the Form. *See supra* note 146.

374 *See* section II.E of this Release.

375 *See* section II.D of this Release.

376 Specifically, the SEC estimated that (1) 3,320 private fund advisers that are currently registered with the SEC will remain registered after certain advisers make the switch to state registration prompted by the Dodd-Frank Act's amendments to section 203A of the Advisers Act, (2) 750 advisers to private funds will register with the Commission as a result of the Dodd-Frank Act's elimination of the private adviser exemption and

will not be required to file Form PF because they have less than $150 million in private fund assets under management.[377] Accordingly, the SEC anticipates that, when advisers begin reporting on Form PF, a total of approximately 3,570 advisers will be required to file all or part of the Form.[378] Out of this total number, the SEC estimates that approximately 3,070 will be smaller private fund advisers, not meeting the thresholds as Large Private Fund Advisers.[379] Commenters did not address the SEC's estimates of the total number of respondents or the number of smaller private fund advisers.[380]

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(3) 200 additional advisers to private funds will register in the next year. *See* Implementing Adopting Release, *supra* note 11, at n.637 and accompanying text. Estimates of registered private fund advisers are based in part on the number of advisers that reported a fund in Section 7.B of Schedule D to the version of Form ADV in use prior to the date of this release. Because these responses included funds that the adviser's related persons manage as well as those the adviser itself manages, these data may over-estimate the total number of private fund advisers.

377 Based on IARD data as of October 1, 2011. *See supra* section II.A of this Release for a discussion of the minimum reporting threshold.

378 4,270 total private fund advisers – 700 with less than $150 million in private fund assets under management = 3,570 advisers. The SEC notes, however, that if a private fund is advised by both an adviser and one or more subadvisers, only one of these advisers is required to complete Form PF. *See* section II.A.6 of this Release. As a result, it is likely that some portion of these advisers either will not be required to file Form PF or will be subject to a reporting burden lower than is estimated for purposes of this PRA analysis. The SEC has not attempted to adjust the burden estimates downward for this purpose because the SEC does not currently have reliable data with which to estimate the number of funds that have subadvisers.

379 Based on the estimated total number of registered private fund advisers that would not meet the thresholds to be considered Large Private Fund Advisers. (3,570 estimated registered private fund advisers – 250 large hedge fund advisers – 80 large liquidity fund advisers – 170 large private equity fund advisers = 3,070 smaller private fund advisers.)

380 The SEC has updated these estimates to reflect: (1) updated data from IARD, (2) the addition of a minimum reporting threshold of $150 million in private fund assets, which reduces the number of advisers subject to the reporting requirements, and (3) the revised estimates of large hedge fund advisers and large private equity advisers discussed in section II.A.4 of this Release. *See supra* section II.A of this Release and notes 88 and 89.

Smaller private fund advisers must complete all or portions of section 1 of Form PF and file on an annual basis. As discussed in greater detail above, section 1 requires basic data regarding the reporting adviser's identity and certain information about the private funds it manages, such as performance, leverage and investor data.[381] If the reporting adviser manages any hedge funds, section 1 also requires basic information regarding those funds, including their investment strategies, counterparty exposures and trading and clearing practices.

The SEC estimates that smaller private fund advisers will require an average of approximately 40 burden hours to compile, review and electronically file the required information in section 1 of Form PF for the initial filing and an average of approximately 15 burden hours for subsequent filings.[382] These estimates reflect an increase compared to the proposal from 10 to 40 hours for the initial filing and from 3 to 15 hours for subsequent filings.

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381 *See supra* section II.C.1.

382 These estimates are based, in part, on the SEC's understanding that much of the information in sections 1a and 1b of Form PF is currently maintained by most private fund advisers in the ordinary course of business. *See supra* note 146. In addition, the SEC expects the time required to determine the amount of the adviser's assets under management that relate to private funds of various types to be largely included in the approved burden associated with the SEC's Form ADV. As a result, responding to questions on Form PF that relate to assets under management and determining whether an adviser is a Large Private Fund Adviser should impose little or no additional burden on private fund advisers. Of course, not all questions on Form PF impose the same burden, and the burden of responding to questions may vary substantially from adviser to adviser. These estimates are intended to reflect *averages* for compiling, reviewing and filing the Form, do not indicate the time that may be spent on specific questions and may not reflect the time spent by an individual adviser.

The SEC has increased these estimates to reflect comments suggesting that the estimates included in the proposal were too low.[383] Commenters did not provide alternative estimates for these burdens. However, commenters addressing the large hedge fund adviser burdens did provide alternative estimates.[384] As discussed below, the SEC is also increasing its hour burden estimates with respect to large hedge fund advisers based on, among other things, the estimates these commenters provided.[385] In the absence of specific commenter estimates for the smaller adviser reporting burden, the SEC has, therefore, scaled these estimates in proportion to the increases it is making to its burden hour estimates for large hedge fund advisers.

Although the SEC has increased these estimates, it has also taken into account changes from the proposal that it expects, on the whole, to mitigate the burden of reporting the information required in section 1. For instance, we have modified the requirement to report performance by allowing advisers to report monthly and quarterly results only if such results are already calculated for the fund.[386] In addition, we have removed from section 1b a question requiring identification of significant creditors and

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383 *See, e.g.*, AIMA General Letter; IAA Letter; SIFMA Letter.

384 *See, e.g.*, MFA Letter.

385 *See infra* section IV.B of this Release.

386 Several commenters argued that carrying out valuations to report monthly and quarterly performance for private equity funds would result in significant cost burdens and require significantly more time than was estimated. *See, e.g.*, comment letter of Atlas Holdings (March 9, 2011) ("Atlas Letter"); PEGCC Letter. We have, however, modified the reporting requirements so that advisers only need to provide monthly and quarterly performance results to the extent already calculated. *See supra* notes 198-202 and accompanying text. In other words, because advisers will have always already calculated the required performance data for purposes other than reporting on Form PF, the burden of reporting it on the Form is essentially one of data entry.

substantially reduced the amount of information required with respect to trading and clearing practices in section 1c.[387] We have also made several global changes to the Form that we anticipate will reduce the burden of reporting. These include the removal of the certification, the increased ability of advisers to rely on their existing methodologies and recordkeeping practices and allowing advisers to omit information regarding parallel managed accounts from their responses to the Form.[388] We have also added four new questions in section 1b that will increase the burden of completing that portion of the Form, but the SEC expects the other changes described above to result in a net reduction in the burden of completing the Form relative to the proposal.[389]

Based on the foregoing, the SEC estimates that the amortized average annual

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387 One commenter suggested the question we removed would have been "very burdensome." *See* PEGCC Letter.

388 *See, e.g.*, *supra* section II.C.5 of this Release and notes 183-188 and accompanying text.

389 *See supra* section II.C.1 of this Release. The SEC originally proposed one of the new questions on Form ADV, and it requires that advisers report the assets and liabilities of each fund broken down using categories that are based on the fair value hierarchy established under GAAP. For advisers obtaining fund audits in accordance with GAAP or a similar international accounting standard, the burden of this question is simply that of entering the data on the Form. In the Implementing Adopting Release, the SEC estimated that approximately 3% of registered advisers have at least one private fund client that may not be audited. *See* Implementing Adopting Release, *supra* note 11, at nn. 634-636 and accompanying text. For this sub-group of advisers, the cost and hour burdens of determining fair values for the funds' assets have already been accounted for in connection with Form ADV because advisers are required to report regulatory assets under management in that form using the fair value of private fund assets. *See* Implementing Adopting Release, *supra* note 11, at section VI and nn. 632-641 and 723 and accompanying text. The question does not require advisers to determine the fair value of liabilities for which they do not already make such determination, so this sub-group of advisers would not incur an incremental cost to fair value liabilities in order to respond to this question. This sub-group of advisers may incur an additional hours burden to determine the categories applicable to the fund's assets and liabilities, and in determining to increase its average hour burden estimates for both smaller private fund advisers and Large Private Fund Advisers, the SEC has taken into account the contribution of this additional hours burden.

burden of periodic filings will be 23 hours per smaller private fund adviser for each of the first three years,[390] and the amortized aggregate annual burden of periodic filings for smaller private fund advisers will be 70,600 hours for each of the first three years.[391]

B. Burden Estimates for Large Hedge Fund Advisers

The SEC estimates that 250 advisers will be classified as large hedge fund advisers.[392] As discussed above, large hedge fund advisers must complete section 1 of the Form and provide additional information regarding the hedge funds they manage in section 2 of the Form. These advisers must report information regarding the hedge funds they manage on a quarterly basis.

Because large hedge fund advisers generally must report more information on Form PF than other private fund advisers, the SEC estimates that these advisers will require, on average, more hours than other Large Private Fund Advisers to configure systems and to compile, review and electronically file the required information. Accordingly, the SEC estimates that large hedge fund advisers will require an average of approximately 300 burden hours for an initial filing and 140 burden hours for each subsequent filing.[393]

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390 The SEC estimates that a smaller private fund adviser will make 3 annual filings in three years, for an amortized average annual burden of 23 hours (1 initial filing x 40 hours + 2 subsequent filings x 15 hours = 70 hours; and 70 hours ÷ 3 years = approximately 23 hours). After the first three years, filers generally will not incur the start-up burdens applicable to the first filing.

391 23 burden hours on average per year x 3,070 smaller private fund advisers = 70,600 burden hours per year.

392 *See supra* note 88.

393 The estimates of hour burdens and costs for large hedge fund advisers provided in the Paperwork Reduction Act and cost-benefit analyses are based, in part, on burden data that advisers provided in response to the FSA Survey and on the experience of SEC staff.

These estimates reflect an increase compared to the proposal from 75 to 300 hours for the initial filing and from 35 to 140 hours for subsequent filings. The SEC has increased these estimates to reflect comments suggesting that the estimates included in the proposal were too low.[394] One industry group reported that some members attempted to complete the proposed version of Form PF for one or more funds and, "[b]ased on their experience, and recognizing that efficiencies will develop over time, [this group estimated] that large managers on average will expend 150-300 hours to submit the initial Form."[395] The SEC has revised its estimates in this PRA analysis based on the top end of

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These estimates also assume that some Large Private Fund Advisers will find it efficient to automate some portion of the reporting process, which will increase the burden of the initial filing but reduce the burden of subsequent filings. This efficiency gain is reflected in our burden estimates, which are higher for the first report than subsequent reports, and certain of the anticipated automation costs are accounted for in our cost estimates. *See infra* note 435 and accompanying text. Of course, not all questions on Form PF impose the same burden, and the burden of responding to questions may vary substantially from adviser to adviser. These estimates are intended to reflect *averages* for compiling, reviewing and filing the Form, do not indicate the time that may be spent on specific questions and may not reflect the time spent by an individual adviser.

394 *See, e.g.*, AIMA Letter; IAA Letter; Kleinberg General Letter; MFA Letter; TCW Letter.

395 MFA Letter. This commenter referred to "large managers" generally, but based on the context, this comment appears to relate to large hedge fund advisers specifically. This commenter went on to state that "managers with more complex strategies will expend considerably more time." Other commenters addressing these estimates did not provide alternative estimates, though one indicated that some clients had already exceeded the Proposing Release's estimates in preparing to report on the proposed Form and another commenter, itself one of the largest private fund advisers in the United States, argued that the estimates were understated by "orders of magnitude." *See* BlackRock Letter; *see also* Kleinberg General Letter. In addition, advisers that manage many funds may incur higher costs than advisers that manage fewer funds even if they manage similar amounts of assets. The SEC's estimates are intended to reflect *average* burdens, and it recognizes that particular advisers may, based on their circumstances, incur burdens substantially greater than or less than the estimated averages. In addition, we have based our estimates in part on data that advisers provided in response to the FSA Survey regarding the time required to complete that survey. Although Form PF generally requires more information regarding hedge funds than the FSA Survey, the SEC believes, based on this data and based on the MFA comment letter, that the *average* burden of completing Form PF is very unlikely to be in the thousands or tens of thousands of hours.

this range, which represents a conservative interpretation of this commenter's estimate. This approach appears justified in this case based on other comments suggesting that the hours burden imposed on these advisers could be significantly higher than the SEC estimated in the Proposing Release.[396]

The SEC notes, however, that this commenter's estimates were based on the Form as proposed and we have made a number of changes from the proposal that we expect, on the whole, to mitigate significantly the reporting burden. For example, we have modified a number of questions to reduce the amount of detail required or to allow advisers to rely more on their existing methodologies or recordkeeping practices, including questions regarding trading and clearing practices, interest rate sensitivities, geographical concentrations, turnover, collateral practices, CCP exposures and sensitivities to changes in specified market factors.[397] We have also made several global changes to the Form that we anticipate will reduce the burden of reporting. These include allowing large hedge fund advisers to report only annually on funds that are not hedge funds, the removal of the certification, expanding the ability to disregard funds of funds and allowing advisers to omit information regarding parallel managed accounts from their responses to the Form.[398] We have also added four new questions in section 1b, which will increase the burden of completing that portion of the Form.[399] The SEC believes, however, that the increased burden attributable to these new questions is less than the

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396 *See supra* note 394 and accompanying text.

397 *See supra* section II.C.1 and II.C.2 of this Release.

398 *See, e.g., supra* sections II.B.1 and II.C.5 of this Release and notes 129 and 183-188 and accompanying text.

399 *See supra* section II.C.1.

reduced burden attributable to other changes to the Form because the new questions require limited information that, in many cases, will be readily available to advisers while some of the SEC's modifications to reduce the reporting burdens are intended to address areas of the Form that commenters identified as particularly burdensome. In light of these changes, the SEC believes that the commenter estimates, which were based on the proposed Form, likely represent an upper bound of the average burden to large hedge fund advisers.

Based on the foregoing, the SEC estimates that the amortized average annual burden of periodic filings will be 610 hours per large hedge fund adviser for each of the first three years.[400] In the aggregate, the amortized annual burden of periodic filings will then be 153,000 hours for large hedge fund advisers for each of the first three years.[401]

C. Burden Estimates for Large Liquidity Fund Advisers

The SEC estimates that 80 advisers will be classified as large liquidity fund advisers.[402] Commenters did not address this estimate. As discussed above, large liquidity fund advisers must complete section 1 of the Form and provide additional information regarding the liquidity funds they manage in section 3 of the Form. In addition, these advisers must report information regarding the liquidity funds they manage on a quarterly basis.

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400 The SEC estimates that a large hedge fund adviser will make 12 quarterly filings in three years, for an amortized average annual burden of 610 hours (1 initial filing x 300 hours + 11 subsequent filings x 140 hours = 1,840 hours; and 1,840 hours ÷ 3 years = approximately 610 hours). After the first three years, filers generally will not incur the start-up burdens applicable to the first filing.

401 610 burden hours on average per year x 250 large hedge fund advisers = 153,000 hours.

402 *See supra* note 88.

Large liquidity fund advisers generally must report less information on Form PF than large hedge fund advisers but more information than large private equity advisers and smaller private fund advisers. Accordingly, the SEC estimates that large liquidity fund advisers will require, on average, fewer hours than large hedge fund advisers but more hours than other advisers to configure systems and to compile, review and electronically file the required information. Specifically, the SEC estimates these advisers will require an average of approximately 140 burden hours for an initial filing and 65 burden hours for each subsequent filing.[403]

These estimates reflect an increase compared to the proposal from 35 to 140 hours for the initial filing and from 16 to 65 hours for subsequent filings. The SEC has increased these estimates to reflect comments suggesting that the estimates included in the proposal were too low.[404] Commenters did not provide alternative estimates for these burdens. However, commenters addressing the large hedge fund adviser burdens did

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403 The estimates of hour burdens and costs for large liquidity fund advisers provided in the Paperwork Reduction Act and cost-benefit analyses are based, in part, on a comparison to the requirements and estimated burden for large hedge fund advisers (which estimates, in turn, are based in part on burden data that advisers provided in response to the FSA Survey) and on the experience of SEC staff. These estimates also assume that some Large Private Fund Advisers will find it efficient to automate some portion of the reporting process, which will increase the burden of the initial filing but reduce the burden of subsequent filings. This efficiency gain is reflected in our burden estimates, which are higher for the first report than subsequent reports, and certain of the anticipated automation costs are accounted for in our cost estimates. *See infra* note 435 and accompanying text. Of course, not all questions on Form PF impose the same burden, and the burden of responding to questions may vary substantially from adviser to adviser. These estimates are intended to reflect *averages* for compiling, reviewing and filing the Form, do not indicate the time that may be spent on specific questions and may not reflect the time spent by an individual adviser.

404 *See*, *e.g.*, AIMA Letter; IAA Letter; BlackRock Letter. No commenters specifically addressed the burden estimates for liquidity fund advisers, though several commented on the burden estimates generally.

provide alternative estimates.[405] As discussed above, the SEC is also increasing its hour burden estimates with respect to large hedge fund advisers based on, among other things, the estimates these commenters provided.[406] In the absence of specific commenter estimates for the large liquidity fund adviser reporting burden, the SEC has, therefore, scaled these estimates in proportion to the increases it is making to its burden hour estimates for large hedge fund advisers.

Although the SEC has increased these estimates, it has also taken into account changes from the proposal that it expects, on the whole, to mitigate the burden of reporting for large liquidity fund advisers. For instance, we have eliminated from section 1b a question requiring identification of significant creditors.[407] We have also made several global changes that we anticipate will reduce the burden of reporting. These include allowing large liquidity fund advisers to report only annually on funds that are not liquidity funds, removing the certification, expanding the ability to disregard funds of funds, the increased ability of advisers to rely on their existing methodologies and recordkeeping practices and allowing advisers to omit information regarding parallel managed accounts from their responses to the Form.[408] We have also added four new questions in section 1b that will increase the burden of completing that portion of the

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405 *See, e.g.*, MFA Letter.

406 *See supra* section IV.B of this Release.

407 *See supra* section II.C.1 of this Release. One commenter suggested the question we removed would have been "very burdensome." *See* PEGCC Letter.

408 *See, e.g.*, *supra* sections II.B.1 and II.C.5 of this Release and notes 129 and 183-188 and accompanying text.

Form, but the SEC expects the other changes described above to result in a net reduction in the burden of completing the Form relative to the proposal.[409]

Based on the foregoing, the SEC estimates that the amortized average annual burden of periodic filings will be 290 hours per large liquidity fund adviser for each of the first three years.[410] In the aggregate, the amortized annual burden of periodic filings will then be 23,200 hours for large liquidity fund advisers for each of the first three years.[411]

D. Burden Estimates for Large Private Equity Advisers

The SEC estimates that 170 advisers will be classified as large private equity advisers.[412] As discussed above, large private equity advisers must complete section 1 of the Form and provide additional information regarding the private equity funds they manage in section 4 of the Form. These advisers are only required to report on an annual basis.

Large private equity advisers generally must report less information on Form PF than other Large Private Fund Advisers but more information than smaller private fund advisers. Accordingly, the SEC estimates that large private equity advisers will require, on average, fewer hours than large hedge fund advisers and large liquidity fund advisers

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409 *See supra* section II.C.1 of this Release.

410 The SEC estimates that a large liquidity fund adviser will make 12 quarterly filings in three years, for an amortized average annual burden of 290 hours (1 initial filing x 140 hours + 11 subsequent filings x 65 hours = 855 hours; and 855 hours ÷ 3 years = approximately 290 hours). After the first three years, filers generally will not incur the start-up burdens applicable to the first filing.

411 290 burden hours on average per year x 80 large hedge fund advisers = 23,200 hours.

412 *See supra* note 89.

but more hours than other advisers to configure systems and to compile, review and electronically file the required information. Specifically, the SEC estimates these advisers will require an average of approximately 100 burden hours for an initial filing and 50 burden hours for each subsequent filing.[413]

These estimates reflect an increase compared to the proposal from 25 to 100 hours for the initial filing and from 12 to 50 hours for subsequent filings. The SEC has increased these estimates to reflect comments suggesting that the estimates included in the proposal were too low.[414] Commenters did not provide alternative estimates for these burdens. However, commenters addressing the large hedge fund adviser burdens did provide alternative estimates.[415] As discussed above, the SEC is also increasing its hour burden estimates with respect to large hedge fund advisers based on, among other things, the estimates these commenters provided.[416] In the absence of specific commenter estimates for the large private equity adviser reporting burden, the SEC has, therefore,

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413 The estimates of hour burdens and costs for large private equity advisers provided in the Paperwork Reduction Act and cost-benefit analyses are based, in part, on a comparison to the requirements and estimated burden for large hedge fund advisers (which estimates, in turn, are based in part on burden data that advisers provided in response to the FSA Survey) and on the experience of SEC staff. These estimates also assume that some Large Private Fund Advisers will find it efficient to automate some portion of the reporting process, which will increase the burden of the initial filing but reduce the burden of subsequent filings. This efficiency gain is reflected in our burden estimates, which are higher for the first report than subsequent reports, and certain of the anticipated automation costs are accounted for in our cost estimates. *See infra* note 435 and accompanying text. Of course, not all questions on Form PF impose the same burden, and the burden of responding to questions may vary substantially from adviser to adviser. These estimates are intended to reflect *averages* for compiling, reviewing and filing the Form, do not indicate the time that may be spent on specific questions and may not reflect the time spent by an individual adviser.

414 *See, e.g.*, Atlas Letter; PEGCC Letter; USCC Letter.

415 *See, e.g.*, MFA Letter.

416 *See supra* section IV.B of this Release.

scaled these estimates in proportion to the increases it is making to its burden hour estimates for large hedge fund advisers.

Although the SEC has increased these estimates, it has also taken into account changes from the proposal that it expects, on the whole, to mitigate the burden of reporting for large private equity advisers. For instance, we have modified the requirement to report performance by allowing advisers to report monthly and quarterly results only if such results are already calculated for the fund.[417] In addition, we have eliminated from section 1b a question requiring identification of significant creditors and have revised questions in section 4 requiring information regarding portfolio company leverage to align the information required more closely with information available on the balance sheets of those companies.[418] We have also made several global changes to the Form that we anticipate will reduce the burden of reporting. These include requiring only annual (rather than quarterly) reporting, removing the certification, expanding the ability to disregard funds of funds, increasing the ability of advisers to rely on their existing methodologies and recordkeeping practices and allowing advisers to omit information regarding parallel managed accounts from their responses to the Form.[419] We have also added four new questions in section 1b that will increase the burden of completing that

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417 *See supra* note 386.

418 *See supra* sections II.C.1 and II.C.4 of this Release. One commenter suggested the question we removed would have been "very burdensome." *See* PEGCC Letter.

419 *See, e.g.*, *supra* sections II.B.1 and II.C.5 of this Release and notes 129 and 183-188 and accompanying text.

portion of the Form, but the SEC expects the other changes described above to result in a net reduction in the burden of completing the Form relative to the proposal.[420]

Based on the foregoing, the SEC estimates that the amortized average annual burden of periodic filings will be 67 hours per large private equity adviser for each of the first three years.[421] In the aggregate, the amortized annual burden of periodic filings will then be 11,400 hours for large private equity advisers for each of the first three years.[422]

E. Burden Estimates for Transition Filings, Final Filings and Temporary Hardship Exemption Requests

In addition to periodic filings, a private fund adviser must file very limited information on Form PF in three situations.

First, any adviser that transitions from quarterly to annual filing because it has ceased to be a large hedge fund or large liquidity fund adviser must file a Form PF indicating that it is no longer obligated to report on a quarterly basis. The SEC estimates that approximately 9 percent of quarterly filers will need to make a transition filing each year with a burden of 0.25 hours, or a total of 7 burden hours per year for all private fund advisers.[423] No commenters addressed these estimates. The SEC has not changed its

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420 *See supra* section II.C.1 of this Release.

421 The SEC estimates that a large private equity adviser will make 3 annual filings in three years, for an amortized average annual burden of 67 hours (1 initial filing x 100 hours + 2 subsequent filings x 50 hours = 200 hours; and 200 hours ÷ 3 years = approximately 67 hours). After the first three years, filers generally will not incur the start-up burdens applicable to the first filing.

422 67 burden hours on average per year x 170 large private equity advisers = 11,400 hours.

423 This estimate is based on IARD data on the frequency of advisers to one or more private funds ceasing to have assets under management sufficient to cause them to be large hedge fund or large liquidity fund advisers. ((80 large liquidity fund advisers + 250 large hedge fund advisers) x 0.09 x 0.25 hours = 7 hours.)

estimates of the rate of transition filings and the burden hours per filing from the proposal, but it has reduced its estimate of the total burden hours per year because fewer filers will be required to report on a quarterly basis.[424]

Second, filers who are no longer subject to Form PF's periodic reporting requirements must file a final report indicating that fact. The SEC estimates that approximately 8 percent of the advisers required to file Form PF will have to file such a report each year with a burden of 0.25 of an hour, or a total of 71 burden hours per year for all private fund advisers.[425] No commenters addressed these estimates. The SEC has not changed its estimates of the rate of final filings and the burden hours per filing from the proposal, but it has reduced its estimate of the total burden hours per year because the addition of a minimum reporting threshold will result in fewer filers reporting on Form PF.[426]

Finally, an adviser experiencing technical difficulties in submitting Form PF may request a temporary hardship exemption by filing portions of Form PF in paper format.[427] The information that must be filed is comparable to the information that Form ADV filers provide on Form ADV-H when requesting a temporary hardship exemption relating to that form. In the case of Form ADV-H, the SEC has estimated that the average burden of

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424 Under the proposal, large private equity advisers would also have been required to file on a quarterly basis. *See supra* section II.B.1 of this Release.

425 Estimate is based on IARD data on the frequency of advisers to one or more private funds withdrawing from SEC registration. (3,570 private fund advisers x 0.08 x 0.25 hours = 71 hours.)

426 *See supra* section II.A of this Release.

427 *See* Advisers Act rule 204(b)-1(f). The rule requires that the adviser complete and file Item A of Section 1a and Section 5 of Form PF, checking the box in Section 1a indicating that the filing is a request for a temporary hardship exemption.

filing is 1 hour and that approximately 1 in every 1,000 advisers will file annually.[428] Assuming that Form PF filers request hardship exemptions at the same rate and that the applications impose the same burden per filing, the SEC expects approximately 4 filers to request a temporary hardship exemption each year[429] for a total of 4 burden hours.[430] No commenters addressed these estimates, and they remain unchanged from the proposal.

F. Aggregate Hour Burden Estimates

Based on the foregoing, the SEC estimates that Form PF would result in an aggregate of 258,000 burden hours per year for all private fund advisers for each of the first three years, or 72 burden hours per year on average for each private fund adviser over the same period.[431]

G. Cost Burden

In addition to the hour burdens identified above, advisers subject to the Form PF reporting requirements will incur cost burdens. Firms required to file Form PF must also pay filing fees. In a separate order, the SEC has established filing fees for the Form PF filing system of $150 per annual filing and $150 per quarterly filing.[432] We estimate that

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428 *See* Implementing Adopting Release, *supra* note 11, at section VI.F.

429 3,570 private fund advisers x 1 request per 1,000 advisers = approximately 4 advisers.

430 4 advisers x 1 hour per response = 4 hours.

431 70,600 hours for periodic filings by smaller advisers + 153,000 hours for periodic filings by large hedge fund advisers + 23,200 hours for periodic filings by large liquidity fund advisers + 11,400 hours for periodic filings by large private equity fund advisers + 7 hours per year for transition filings + 71 hours per year for final filings + 4 hours per year for temporary hardship requests = approximately 258,000 hours per year. 258,000 hours per year ÷ 3,570 total advisers = 72 hours per year on average.

432 *See supra* section II.E of this Release.

this will result in advisers paying aggregate filing fees of approximately $684,000 per year.[433]

Several commenters suggested that advisers would also need to modify existing systems or deploy new systems to support Form PF reporting.[434] As discussed in the Proposing Release and below, the SEC acknowledges that advisers may incur costs to develop systems and expects that Large Private Fund Advisers, in particular, may find it efficient to automate some portion of the reporting process, which will increase the burden of the initial filing but reduce the burden of subsequent filings.[435] The SEC has assumed that some of the hours that it estimates advisers will spend on preparing their initial filings on Form PF will be attributable to programmers preparing systems for the reporting.[436] The SEC understands that some advisers may outsource all or a portion of these systems requirements to software consultants, vendors, filing agents or other third-party service providers and believes that the emergence of such service providers may serve to make filing on Form PF more efficient than is reflected in its estimates.[437]

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433 ((3,070 smaller private fund advisers + 170 large private equity advisers) x $150 per annual filing) + ((250 large hedge fund advisers + 80 large private equity advisers) x $150 per quarterly filing x 4 quarterly filings per year) = $684,000 per year.

434 *See*, *e.g.*, BlackRock Letter; IAA Letter; Kleinberg General Letter; PEGCC Letter; SIFMA Letter.

435 *See infra* section V.B of this Release, especially nn. 511-515; Proposing Release, *supra* note 11, at section V.B.

436 *See infra* notes 511, 513 and 515.

437 The SEC has based its estimates on the use of internal resources, for which some cost data is available, because it believes that an adviser would engage third-party service providers only if the external costs were comparable, or less than, the estimated internal costs of compiling, reviewing and filing the Form PF. As a result, the SEC's estimates of hour and cost burdens in this PRA analysis, and of costs in section V.B of this Release, may overstate the actual burdens and costs that will be incurred once third-party services become available.

Advisers may also incur costs associated with the acquisition or use of hardware needed to perform computations or otherwise process the data required on Form PF.[438] Smaller private fund advisers are unlikely to bear these costs because the information they are required to provide is limited and will, in many cases, already be maintained in the ordinary course of business.[439] Even among Large Private Fund Advisers, these costs are likely to vary significantly. For instance, the cost to any Large Private Fund Adviser may depend on how many funds or the types of funds it manages, the state of its existing systems and the complexity of its business. In addition, large hedge fund and large liquidity fund advisers must file Form PF more frequently, on shorter deadlines and generally with more information than large private equity advisers, increasing the likelihood that filings will compete with other demands for computing resources and that additional resources will be required.

Commenters did not provide estimates for the costs of acquiring or using hardware for purposes of Form PF. SEC staff contacted several organizations, including self-regulatory organizations, prime brokers and fund service providers, to help develop an estimate for these costs. Although these organizations generally were not able to provide such estimates, some expressed the view that the hardware costs would be small relative to the human capital costs and, for Large Private Fund Advisers, software development costs that Form PF imposes.[440] The SEC estimates, based in part on these conversations and the factors discussed above, that these costs will fall across a broad

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438 *See supra* note 272.

439 *See supra* note 382.

440 *See supra* notes 435-436 and accompanying text.

range for Large Private Fund Advisers. Those who are required to file less information, less frequently and on longer deadlines, who have excess capacity in their existing systems or whose business is relatively simple, may incur no incremental hardware costs. On the other hand, some Large Private Fund Advisers may need to acquire (or obtain the use of) computing resources equivalent to an additional server, which the SEC estimates would cost approximately $50,000 fully deployed. This suggests an aggregate incremental cost in the first year of reporting between $0 and $25,000,000, though the actual cost is likely to fall in between these two end-points.[441]

CFTC:

As adopted, CEA rule 4.27 does not impose any additional burden upon registered CPOs and CTAs that are dually registered as investment advisers with the SEC. By filing the Form PF with the SEC, these dual registrants would be deemed to have satisfied certain of their filing obligations with the CFTC should the CFTC adopt such requirements, and the CFTC is not imposing any additional burdens herein. Therefore, any burden imposed by Form PF through CEA rule 4.27 on entities registered with both the CFTC and the SEC has been accounted for within the SEC's calculations regarding the impact of this collection of information under the PRA or, to the extent the reporting may relate to commodity pools that are not private funds, the CFTC anticipates that it would account for this burden should it adopt a future rulemaking establishing reporting requirements with respect to those commodity pools.[442]

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441 $50,000 x 500 Large Private Fund Advisers = $25,000,000.

442 44 U.S.C. 3501-3521.

V. ECONOMIC ANALYSIS

As discussed above, the Dodd-Frank Act amended the Advisers Act to, among other things, authorize the SEC to promulgate reporting requirements for private fund advisers. The Dodd-Frank Act also directs the SEC and CFTC to jointly issue, after consultation with FSOC, rules establishing the form and content of any reports to be filed under this new authority.[443] In enacting Sections 404 and 406 of the Dodd-Frank Act, Congress determined to require that private fund advisers file reports with the SEC and specified certain types of information that should be subject to reporting and/or recordkeeping requirements, but Congress left to the SEC the determination of the specific information to be maintained or reported. When determining the form and content of such reports, the Dodd-Frank Act authorizes the SEC to require that private fund advisers file such information "as necessary and appropriate in the public interest and for the protection of investors, or for the assessment of system risk by [FSOC]."[444]

The SEC is adopting Advisers Act rule 204(b)-1 and Form PF, and the CFTC is adopting CEA rule 4.27 and sections 1 and 2 of Form PF, to implement the private fund adviser reporting requirements that the Dodd-Frank Act directs the Commissions to promulgate. Under these new rules, private fund advisers having at least $150 million in private fund assets under management must file with the SEC information responsive to all or portions of Form PF on a periodic basis. The scope of the required information and the frequency of the reporting is related to the amount of private fund assets that each

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443 *See* section 211(e) of the Advisers Act.

444 *See* section 204(b)(1)(A) of the Advisers Act.

private fund adviser manages and the types of private fund to which those assets relate.[445] Specifically, smaller private fund advisers must report annually and provide only basic information regarding their operations and the private funds they advise. Large private equity advisers also must report on an annual basis but are required to provide additional information with respect to the private equity funds they manage. Finally, large hedge fund advisers and large liquidity fund advisers must report on a quarterly basis and provide more information than other private fund advisers.

The Advisers Act directs the SEC, when engaging in rulemaking that requires it to consider or determine whether an action is necessary or appropriate in the public interest, to consider, in addition to the protection of investors, whether the action will promote efficiency, competition and capital formation.[446] The Commissions are sensitive to the costs and benefits of their respective rules and have carefully considered the costs and benefits of this rulemaking. The SEC's consideration of the costs and benefits of this rulemaking has included whether this rulemaking will promote efficiency, competition and capital formation. In the proposal, the Commissions identified certain costs and benefits of Advisers Act rule 204(b)-1, CEA rule 4.27 and Form PF and requested comment on all aspects of their cost-benefit analyses. The comments the Commissions received on those analyses are discussed below.

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445 *See* section II.A of this Release (describing who must file Form PF); *see also* section II.B of this Release (discussing the frequency with which private fund advisers must file Form PF); section II.C of this Release (describing the information that private fund advisers must report on Form PF). *See also* proposed Instruction 9 to Form PF for information regarding the frequency with which private fund advisers must file Form PF.

446 *See* section 202(c) of the Advisers Act.

In considering the benefits and costs of this rulemaking, we have also considered alternatives to the requirements we are adopting. All of these alternatives would require at least some registered private fund advisers to report at least some information because Congress directed the SEC to adopt such reporting requirements. Among the alternatives that we considered were requirements that varied along the following five dimensions: (1) requiring more or less information; (2) requiring more or fewer advisers to complete the Form; (3) allowing advisers to rely more on their existing methodologies and recordkeeping practices in completing the Form (or, alternatively, requiring more standardized responses); (4) requiring more or less frequent reporting; and (5) allowing advisers more or less time to complete and file the Form.

Alternatives along each of these dimensions have advantages and disadvantages. Obtaining more standardized information from more advisers more often and more quickly would likely improve the value of the Form PF data to FSOC and other regulators, and several commenters supported alternatives along one or more of these dimensions.[447] The Commissions are concerned, however, that the costs of such changes may, in general, increase more quickly than the benefits.[448] On the other hand, the Commissions have considered, and are adopting changes from the proposal, that allow advisers more time to file the Form,[449] permit large private equity advisers to file less

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447 *See, e.g.*, AFL-CIO Letter; AFR Letter. *See also* CII Letter; MSCI Letter.

448 *See, e.g.*, *supra* discussion following notes 101 and 158 and text accompanying note 256. We believe, however, that there are some exceptions, such as the additional information it has determined to request in section 1b of the Form. *See supra* section II.C.1 of this Release.

449 *See supra* section II.B.2 of this Release.

frequently,[450] generally reduce the amount of information required,[451] reduce the number of advisers required to file the Form[452] and allow advisers to rely more on their existing methodologies and recordkeeping practices.[453] A number of commenters supported these changes and, in some cases, would have preferred that we further reduce the reporting burdens.[454] We believe, however, that the approach we are adopting strikes an appropriate balance between the benefits of the information to be collected and the costs to advisers of providing it. These benefits and costs are discussed in greater detail below.

A. Benefits

We believe that Form PF will create two principal classes of benefits. First, the information collected will facilitate FSOC's understanding and monitoring of systemic risk in the private fund industry and assist FSOC in determining whether and how to deploy its regulatory tools with respect to nonbank financial companies. Second, we expect this information to enhance the Commissions' ability to evaluate and develop regulatory policies and improve the efficiency and effectiveness of our efforts to protect investors and maintain fair, orderly and efficient markets.

Congress passed the Dodd-Frank Act in the wake of what some have called "the greatest financial crisis since the Great Depression."[455] The crisis imposed immense

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450 *See supra* section II.B.1 of this Release.

451 *See supra* section II.C of this Release.

452 *See supra* section II.A of this Release.

453 *See supra* section II.C of this Release.

454 *See, e.g.*, IAA Letter; MFA Letter; PEGCC Letter; SIFMA Letter.

455 *The Financial Crisis Inquiry Report: Final Report of the National Commission on the Causes of the Financial and Economic Crisis in the United States*, FINANCIAL CRISIS INQUIRY COMMISSION (Jan. 2011) ("Financial Crisis Inquiry Report") at xv.

costs on individuals and businesses, with millions of jobs disappearing from the U.S. economy, large numbers of families losing their homes to foreclosure, nearly $11 trillion in household wealth lost, including retirement accounts and life savings, and many businesses, large and small, facing serious challenges.[456] Congress responded to the crisis, in part, by establishing FSOC as the center of a framework intended "to prevent a recurrence or mitigate the impact of financial crises that could cripple financial markets and damage the economy."[457] The goal of this framework, in other words, is the avoidance of significant harm to the U.S. economy from future financial crises.

Under the Dodd-Frank Act, FSOC must "monitor emerging risks to U.S. financial stability" and employ its regulatory tools to address those risks.[458] For this purpose, the Dodd-Frank Act granted FSOC the ability to determine that a nonbank financial company will be subject to the supervision of the FRB if the company may pose risks to U.S. financial stability as a result of its activities or in the event of its material financial distress. FSOC may also recommend to the FRB heightened prudential standards for designated nonbank financial companies.[459] In addition, the Dodd-Frank Act authorizes FSOC to issue recommendations to primary financial regulators for more stringent regulation of financial activities that it determines may create or increase systemic risk.[460]

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456 *See id.*, at xv-xvi. *See also* Senate Committee Report, *supra* note 5, at 39.

457 *Id.*

458 *See id.*, at 2. *See also supra* note 6 and accompanying text.

459 *See supra* note 7 and accompanying text.

460 *See supra* note 8 and accompanying text.

Congress recognized that FSOC would need information from private fund advisers to carry out its duties and to determine whether and how to exercise these regulatory authorities. For instance, a Senate committee report noted that "no precise data regarding the size and scope of hedge fund activities are available[, and while] hedge funds are generally not thought to have caused the current financial crisis, information regarding their size, strategies, and positions could be crucial to regulatory attempts to deal with a future crisis."[461] To that end, Congress mandated that the Commissions, as the primary regulators of private fund advisers, gather information from these advisers for FSOC's use. The Commissions have designed Form PF, in consultation with staff representing FSOC's members, to implement this mandate.[462]

Recent releases from FSOC illuminate how Form PF will serve an essential role in FSOC's monitoring of, and exercise of regulatory authority over, the private fund industry. For instance, in one release, FSOC confirmed that the information reported on Form PF is important not only to conducting an assessment of systemic risk among private fund advisers but also to determining how that assessment should be made.[463] Guidance in this FSOC release also suggests the role Form PF data will play in the process of determining whether a private fund adviser or the funds it manages will be subject to FRB supervision.[464] More specifically, the Dodd-Frank Act identifies certain

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461 *See* Senate Committee Report, *supra* note 5, at 38.

462 *See* section II.C of this Release (describing the information that private fund advisers must report on Form PF).

463 *See supra* note 21 and accompanying text.

464 In the proposed three-stage process for making such determinations, the first and second stages would utilize publicly available data and data that, like Form PF, is collected by

factors that FSOC must consider in making a determination to designate a nonbank financial company for FRB supervision, and FSOC's recent guidance organizes those factors into categories, including size, interconnectedness, use of leverage, liquidity risk and maturity mismatch and concentration.[465] As discussed in detail throughout section II.C of this Release, the information reported on Form PF is designed, in part, to provide FSOC with data to assess these factors in a manner that is relevant to the particular type of fund about which the adviser is reporting.[466] Finally, we expect that FSOC will use Form PF data to supplement the data that it collects regarding other financial market participants and gain a broader view of the financial system than is currently available to regulators.[467] In this manner, we believe that the information collected through Form PF could play an important role in FSOC's monitoring of systemic risk, both in the private fund industry and in the financial markets more broadly.

In addition to the content of the Form, the reporting frequency, filing deadlines and reporting thresholds have been designed to provide FSOC the information it needs to monitor systemic risk across the private fund industry while balancing the burdens these reporting requirements will impose on advisers. For instance, although most advisers will only report annually on Form PF, large hedge fund and large liquidity fund advisers will report quarterly because we understand, based on our staffs' consultations with staff

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other regulators. A third stage of screening would generally involve OFR collecting additional, targeted information directly from these firms, which FSOC would analyze along with Form PF data and other data used in the first two stages. *See supra* notes 45-46 and accompanying text.

465 *See* FSOC Second Notice, *supra* note 6.

466 *See, e.g.*, *supra* notes 192, 228, 266, 282, 284, 298 and 323 and accompanying text.

467 *See, e.g.*, Proposing Release, *supra* note 12, at n. 120 and accompanying text.

representing FSOC's members, that this will provide FSOC with timely data that it may use to identify emerging trends in systemic risk.[468] The filing deadlines are, similarly, designed to provide FSOC with timely data so that it may understand and monitor systemic risk on a reasonably current basis.[469] Moreover, as discussed above, the reporting thresholds are designed to provide FSOC with a broad picture of the private fund industry while relieving smaller advisers from much of the costs associated with the more detailed reporting.[470] We understand that obtaining this broad picture will help FSOC to contextualize its analysis and assess whether systemic risk may exist across the private fund industry and to identify areas where OFR may want to obtain additional information.[471]

Certain publications from international groups and researchers have suggested that data like that collected on Form PF will be valuable to the regulation of systemic risk. For instance, as discussed above, several international groups have continued working to close information gaps by increasing the disclosures provided to regulators.[472] These groups have emphasized the importance, in their view, of designing and collecting better information to support the identification and modeling of systemic risk.[473] In

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468 *See supra* section II.B.1 of this Release (discussing reporting frequency and comments on the proposed reporting frequency).

469 *See supra* section II.B.2 of this Release (discussing reporting deadlines and comments on the proposed deadlines).

470 *See supra* section II.A.4.a of this Release (discussing large adviser thresholds and comments on the proposed thresholds). *See also* section II.A of this Release (discussing the minimum reporting thresholds).

471 *Id.*

472 *See supra* notes 28-29 and accompanying text.

473 *Id.*

addition, research papers have suggested that information regarding private funds should play an important role in monitoring systemic risk, and one study argues that more direct measures of systemic risk would be possible with information from the majority of funds in the industry.[474] Another recent research paper argues that expanding the FRB's flow of funds data to include more detailed quarterly information regarding the holding and transfer of financial instruments, including information regarding the portfolios of hedge funds, "would have been of material value to U.S. regulators in ameliorating the recent financial crisis and could be of aid in understanding the potential vulnerabilities of an innovative financial system in the future."[475] Others have commented on hedge fund reporting specifically, stating that "[t]ransparency to regulators can help them measure and manage possible systemic risk and is relatively costless."[476]

Other academics and economists, while supporting regulatory efforts to assess and mitigate systemic risk, have cautioned that achieving the goal of substantially reducing systemic risk may prove difficult. For example, while the authors of one recent work support establishing "early warning indicators" for financial crises, they argue that

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474 *See, e.g.*, Nicholas Chan, Mila Getmansky, Shane Haas and Andrew Lo, *Systemic Risk and Hedge Funds*, in The Risks of Financial Institutions (Mark Carey and Rene Stulz, eds., 2007) at 238; Monica Billio, Mila Getmansky, Andrew Lo and Loriana Pelizzon, *Econometric Measures of Systemic Risk in the Finance and Insurance Sectors*, NATIONAL BUREAU OF ECONOMIC RESEARCH (July 2010).

475 Leonard Nakamura, *Durable Financial Regulation: Monitoring Financial Instruments as a Counterpart to Regulating Financial Institutions*, NATIONAL BUREAU OF ECONOMIC RESEARCH (May 2011) at 1.

476 Stephen Brown, *et al.*, *Hedge Funds, Mutual Funds, and ETFs*, in REGULATING WALL STREET: THE DODD-FRANK ACT AND THE NEW ARCHITECTURE OF GLOBAL FINANCE 360 (Viral V. Acharya, *et al.*, eds., 2011) (supporting "regular and timely" reporting of asset positions and leverage levels). *See also* Ferran, *supra* note 307, at 28.

the most significant challenge is not the design of a framework for systemic risk analysis but rather:

> the well-entrenched tendency of policy makers and market participants to treat the signals as irrelevant archaic residuals of an outdated framework, assuming that old rules of valuation no longer apply. If the past... is any guide, these signals will be dismissed more often than not.[477]

Accordingly, although collecting information on Form PF will increase the transparency of the private fund industry to regulators (an important prerequisite to understanding and monitoring systemic risk), transparency alone may not be sufficient to address systemic risk.[478]

Some commenters agreed that Form PF data will "facilitate FSOC's ability to promote the soundness of the U.S. financial system."[479] One commenter characterized Form PF as determining the extent to which FSOC and the SEC have access to "data essential to monitoring systemic risks that, as we saw in 2007 and 2008, cause substantial damage to the financial markets and the broader economy when they go unchecked."[480] Another commenter stated that Form PF data could aid in the assessment of "systemic

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477 Carmen M. Reinhart and Kenneth S. Rogoff, *This Time is Different: Eight Centuries of Financial Folly* (2009) ("Reinhart and Rogoff") at 277, 280 and 281 (after observing this tendency to disregard signals of systemic risk, the authors conclude that this "is why we also need to think about improving institutions," which may be important to reducing this risk).

478 *See also* FSOC 2011 Annual Report, supra note 19, at ii (explaining that identifying and mitigating potential threats to financial stability "is an inherently difficult exercise. No financial crisis emerges in exactly the same way as its predecessors, and the most significant future threats will often be the ones that are hardest to diagnose and preempt" but going on to state that, "[n]onetheless, there is a strong case for improving the quality of information available to the public, supervisors, and regulators about risks in financial institutions and markets.")

479 CII Letter. *See also, e.g.*, AFL-CIO Letter; AFR Letter.

480 AFL-CIO Letter.

risks due to connectivity and contagion."[481] One commenter who expressed reservations regarding specific aspects of the proposal nonetheless supported "the approach proposed by the SEC and CFTC to collect information from registered private fund managers through periodic, confidential reports on Form PF" and agreed that gathering data "from different types of market participants, including investment advisers and the funds they manage, ...is a critical component of effective systemic risk monitoring and regulation."[482]

Some commenters, however, doubted that Form PF would be beneficial for monitoring systemic risk.[483] One commenter, for instance, argued that "Form PF requires firms to calculate and disclose information with uncertain benefits to regulators, and the broad scope of private funds subject to this burden has not been justified."[484] Others argued that particular types of funds, such as private equity funds, should be excluded from the reporting because they do not, in their view, have the potential to pose systemic risk or that certain of the proposed questions on Form PF would not prove beneficial for systemic risk analysis.[485] As discussed above, based on SEC staff's

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481 MSCI Letter (though also noting that they "see less potential benefit from this exercise to track the formation of asset class bubbles" and that certain of the requested information would be difficult to aggregate for purposes of industry-wide analysis; *see* section II.C for a discussion of some of this commenter's observations regarding use of particular data collected on Form PF).

482 MFA Letter.

483 *See, e.g.*, Fidelity Letter; PEGCC Letter; TCW Letter; USCC Letter.

484 CCMR Letter; *see also* USCC Letter (acknowledging, however, that "greater access to comprehensive market and industry information will assist [FSOC] in identifying emerging threats to the stability of the U.S. financial system."); BlackRock Letter; SIFMA Letter.

485 *See, e.g.*, PEGCC Letter. *See also supra* section II.C of this Release.

consultation with staff representing FSOC's members, we continue to believe that targeted information regarding the leverage practices of private equity funds will provide information that FSOC may use to monitor activities and trends in this industry that are of potential systemic importance.[486] In addition, we have made a number of changes from the proposal intended to address the specific concerns of these commenters and believe that Form PF, as adopted, will be an important source of information for FSOC as it carries out its duties as they relate to the private fund industry.[487]

We cannot predict today what the scope of the next financial crisis will be, and Form PF is only one part of a broader framework established under the Dodd-Frank Act to monitor and address systemic risk.[488] Other measures contemplated by the Dodd-Frank Act, including the so-called "Volcker rule," enhanced regulation of swaps and the FRB's oversight of systemically important financial institutions may be critical to identifying and mitigating the next financial crisis. We anticipate, however, that Form PF will improve the information available to regulators as they seek to prevent or mitigate the effects of future financial crises, and if this information helps to avoid even a small portion of the costs of a financial crisis like the most recent one, the benefits of Form PF will be very significant.

Reporting on Form PF will also benefit investors and other market participants by improving the information available to the Commissions regarding the private fund industry and how it interacts with markets. Today, regulators have little reliable data

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486 *See supra* notes 307-308 and accompanying text.

487 *See supra* section II of this Release (discussing changes from the proposal).

488 *See supra* note 457 and accompanying text.

regarding this rapidly growing sector and frequently have to rely on data from other sources, which when available may be incomplete. The SEC recently adopted amendments to Form ADV that will require the reporting of important information regarding private funds, but this includes little or no information regarding, for instance, performance, leverage or the riskiness of a fund's financial activities.[489] As discussed above, the data collected through Form PF, which will be more reliable than existing data regarding the industry and significantly extend the data available through the revised Form ADV, will assist FSOC in identifying and addressing risks to U.S. financial stability. This may, in turn, protect investors and other market participants from significant losses.

In addition, this data will provide the Commissions with a more complete view of the financial markets in general and the private fund industry in particular. This broader perspective and more reliable data may enhance the Commissions' ability to develop and frame regulatory policies regarding the private fund industry, its advisers and the markets in which they participate, and to more effectively evaluate the outcomes of regulatory policies and programs directed at this sector, including for the protection of private fund investors. For instance, Form PF data may help the Commissions to discern relationships between regulatory actions and private fund results or activities.

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[489] *See* Implementing Adopting Release, *supra* note 11. Information reported on Form ADV is made available to the public, while Form PF data generally will not be. *See supra* section II.D (discussing confidentiality of Form PF data). This has informed the SEC's determination to require certain private fund information on Form ADV and other private fund information on Form PF.

We also expect the Form PF data to improve the efficiency and effectiveness of the Commissions' oversight of private fund advisers by enabling staff to manage and analyze information related to the risks that private funds pose more quickly, more effectively and at a lower cost than is currently possible. This will allow the Commissions to more efficiently and effectively target their examination programs. The Commissions will be able to use Form PF information to generate reports on the industry, its characteristics and trends. We expect that these reports will help the Commissions to anticipate regulatory problems, allocate and reallocate resources, and more fully evaluate and anticipate the implications of various regulatory actions the Commissions may consider taking. This will increase both the efficiency and effectiveness of the Commissions' programs and, thereby, increase investor protection. Form PF data will also help the Commissions better understand the investment activities of private funds and the scope of their potential effect on investors and the markets that the Commissions regulate.

Commenters generally focused on the benefits of Form PF as they relate to systemic risk rather than investor protection. However, one supporter, who represents twelve million workers and sponsors pension and employee benefit plans holding almost half a trillion dollars in assets, agreed that "[c]omprehensive disclosure requirements for private funds will provide important protections for [its] members' retirement savings."[490] On the other hand, some commenters who questioned Form PF's merits expressed skepticism regarding the Form's benefits generally, not just with respect to the

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490 AFL-CIO Letter. *See also* AFR Letter.

monitoring of systemic risk.[491] As discussed in detail above, we have made a number of changes from the proposal designed to address commenter concerns regarding certain aspects of the proposed reporting requirements.[492] However, we continue to believe that Form PF, as adopted, will increase the amount and quality of information available regarding a previously opaque area of investment activity and, thereby, enhance the ability of regulators to protect investors and maintain fair, orderly and efficient markets.

The Commissions believe that private fund advisers, investors in private funds and the companies in which private funds may invest will also enjoy certain benefits related to Form PF. For example, we identified above two principal classes of benefits – assistance to FSOC in carrying out its mission and improvements to the ability of regulators to protect investors and oversee markets – in which these groups will share, including indirectly as participants in the U.S. financial system. With respect to hedge fund advisers, for instance, data indicate that the number of funds shut down each year increased significantly during the recent financial crisis, suggesting that these advisers may benefit if a future financial crisis is averted or mitigated.[493] Private fund investors and private fund advisers will also benefit if reporting on Form PF, by requiring advisers to review their fund's portfolios, trading practices and risk profiles, causes advisers to improve their risk management practices or internal controls.

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491 *See, e.g.*, *supra* note 484.

492 *See supra* section II of this Release (discussing changes from the proposal).

493 *See HedgeFund Intelligence Global Review 2011*, HFI (Spring 2011) ("HFI 2011 Global Review").

Reporting on Form PF may also result in a positive effect on capital formation. Although Form PF data generally will be non-public, Form PF will increase transparency to regulators.[494] The SEC believes that private fund advisers may, as a result, assess more carefully the risks associated with particular investments and, in the aggregate, allocate capital to investments with a higher value to the economy as a whole. To the extent that changes in investment allocations lead to improved economic outcomes in the aggregate, Form PF reporting may result in a positive effect on capital available for investment.

Should the CFTC adopt certain of its proposed systemic risk reporting requirements, the coordination between the CFTC and SEC on this rulemaking would result in significant efficiencies for any private fund adviser that is also registered as a CPO or CTA with the CFTC. This is because, under CEA rule 4.27, filing Form PF would satisfy both SEC and CFTC reporting obligations with respect to commodity pools that are "private funds" and CPOs and CTAs would have the option of reporting on Form PF regarding commodity pools that are not private funds to satisfy certain other CFTC reporting obligations, in each case should the CFTC adopt such reporting obligations.

As discussed in section I.B of this Release, we have also coordinated with foreign financial regulators regarding the reporting of systemic risk information regarding private funds and anticipate that this coordination, as reflected in Form PF, will result in greater efficiencies in private fund reporting, as well as information sharing and private fund

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494 *See supra* section II.D (discussing confidentiality of Form PF data).

monitoring among foreign financial regulators. Ongoing work among various international organizations has emphasized the importance of filling gaps in the data regarding financial market participants, and one goal of this coordination is to collect comparable information regarding private funds, which will aid in the assessment of systemic risk on a global basis.[495] Several commenters agreed that international coordination in connection with private fund reporting is important and encouraged us to take an approach consistent with international precedents.[496] We have made several changes from the proposal intended to more closely align Form PF with international precedent.[497]

As discussed above, we also believe that private fund advisers already collect or calculate some of the information required on the Form at least as often as they must file the Form, creating efficiencies for, and benefiting, advisers in satisfying their reporting requirements.[498]

B. Costs

Reporting on Form PF will also impose certain costs on private fund advisers and, potentially, other market participants. For the most part, these are the same costs discussed in the PRA analysis above because that analysis must account for the burdens of responding to the Commissions' reporting requirements. In order to minimize these direct costs, the reporting requirements are scaled to the adviser's size, the size of funds

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495 *See supra* note 29 and accompanying text.

496 *See supra* note 30 and accompanying text.

497 *See supra* note 35 and accompanying text.

498 *See supra* note 382; Proposing Release, *supra* note 12, at n.105; *but see supra* note 146.

and the types of private funds each adviser manages. For instance, smaller private fund advisers and large private equity advisers generally must report less information and less frequently than large hedge fund advisers and large liquidity fund advisers.[499] This scaled approach is intended to provide FSOC with a broad picture of the private fund industry while relieving smaller advisers from much of the costs associated with the more detailed reporting. It is also designed to reflect the different implications for systemic risk that may be presented by different investment strategies, and thus seeks to adjust the costs of the reporting in proportion to the differing potential benefits of the information reported with respect to these strategies.

We expect that the costs Form PF imposes will be most significant for the first report that a private fund adviser is required to file because the adviser will need to familiarize itself with the new reporting form and may need to configure its systems in order to efficiently gather the required information. We also anticipate that the initial report will require more attention from senior personnel, including compliance managers and senior risk management specialists, than will subsequent reports. In addition, we expect that some Large Private Fund Advisers will find it efficient to automate some portion of the reporting process, which will increase the burden of the initial filing but reduce the burden of subsequent filings.

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499 *See* section II.A of this Release (describing who must file Form PF); section II.B of this Release (discussing the frequency with which private fund advisers must file Form PF); section II.C of this Release (describing the information that private fund advisers must report on Form PF). *See also* Instruction 9 to Form PF (discussing information regarding the frequency with which private fund advisers must file Form PF).

Several commenters addressed the cost estimates included in the Proposing Release. These commenters generally viewed these estimates as understated and, in several cases, argued that the costs of the initial report, in particular, would be greater than assumed.[500] These commenters offered two common explanations for the higher than estimated costs: (1) "[m]any of the requested items on Form PF are not tracked by advisory firms on the frequency, by the category or on a fund-by-fund basis in the manner requested by the proposed Form," meaning that advisers would need to develop systems for the reporting or engage in a manual process of gathering and compiling data;[501] and (2) completing the Form will require gathering information from many different internal and external parties and systems.[502]

We have carefully considered comments suggesting that the reporting requirements would be more burdensome than estimated in the Proposing Release, and the SEC has substantially increased its estimates of the hour burdens included in this PRA analysis, which flow through to these estimates of costs.[503] We have, however, also taken these comments into consideration in making a number of changes from the proposal that are intended to reduce the burdens of reporting on Form PF. These include global changes to the Form, such as allowing most advisers more time to file following the end of a fiscal period (reducing the likelihood that Form PF will compete with other priorities for advisers' resources or require employment of additional personnel),

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500 *See, e.g.*, AIMA Letter; IAA Letter; Kleinberg General Letter; MFA Letter; PEGCC Letter; Seward Letter.

501 TCW Letter; but *see also supra* note 146.

502 *See, e.g.*, Kleinberg General Letter; MFA Letter; PEGCC Letter.

503 *See supra* notes 383, 394-395, 404 and 414 and accompanying text.

extending the compliance date, allowing large private equity advisers to report annually rather than quarterly, increasing the threshold for large private equity advisers and permitting greater reliance on advisers' existing methodologies and recordkeeping practices. We have also modified specific questions in response to comments so that responding to the Form is less burdensome.[504] We expect, on the whole, that these changes will mitigate the cost of reporting.[505] In addition, we have added a minimum reporting threshold, which will not reduce the burden to any particular filer of reporting but will reduce the aggregate burden that Form PF imposes because fewer advisers will be required to report.

After filing their initial reports, we anticipate that advisers will incur significantly lower costs because much of the work involved in the initial report is non-recurring and because of efficiencies realized from system configuration and reporting automation efforts accounted for in the initial reporting period. In addition, we estimate that senior personnel will bear less of the reporting burden in subsequent reporting periods, reducing costs though not necessarily reducing the burden hours.

One commenter agreed that efficiencies will be realized over time,[506] but another stated that, at least for private real estate funds, they would not.[507] Having considered

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504 *See supra* section II.C of this Release.

505 *See supra* notes 388-389, 397-398, 407-409 and 418-420 and accompanying text. We also note that the original cost estimates, as well as the revised estimates included in this Release, include allocations for systems development among Large Private Fund Advisers (who are most likely to find automation cost effective) and assume that information would need to be gathered from many sources, both internal and external. *See supra* note 435 and accompanying text.

506 *See* MFA Letter.

these comments, we continue to believe that, for the average adviser (and particularly for those with more liquid portfolios and greater systems capabilities), efficiencies will be realized over time. We have, however, also increased the cost estimates for subsequent filings in recognition of concerns regarding the overall burden of the reporting and the possibility that efficiencies are not the same for all types of private fund adviser.

Based on the foregoing, we estimate[508] that the periodic filing requirements under Form PF (including configuring systems and compiling, automating, reviewing and electronically filing the report) will impose:

(1) 40 burden hours at a cost of $13,600[509] per smaller private fund adviser for the initial annual report;

(2) 15 burden hours at a cost of $4,200[510] per smaller private fund adviser for each subsequent annual report;

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507 *See* comment letter of The National Association of Real Estate Investment Managers (Mar. 24, 2011).

508 We understand that some advisers may outsource all or a portion of their Form PF reporting responsibilities to software consultants, vendors, filing agents or other third-party service providers. We have based our estimates on the use of internal resources, for which some cost data is available, because we believe that an adviser would engage third-party service providers only if the external costs were comparable, or less than, the estimated internal costs of compiling, reviewing and filing the Form PF. The hourly wage data used in this Economic Analysis section of the Release is based on the Securities Industry and Financial Markets Association's *Report on Management & Professional Earnings in the Securities Industry 2010* and *Office Salaries in the Securities Industry 2010* ("SIFMA Earnings Reports"). This data has been modified to account for an 1,800-hour work-year and multiplied by 5.35 for management and professional employees and by 2.93 for general and compliance clerks to account for bonuses, firm size, employee benefits and overhead.

509 We expect that for the initial report these activities will most likely be performed equally by a compliance manager at a cost of $273 per hour and a senior risk management specialist at a cost of $409 per hour and that, because of the limited scope of information required from smaller private fund advisers, these advisers generally would not realize significant benefits from or incur significant costs for system configuration or automation. ($273/hour x 0.5 + $409/hour x 0.5) x 40 hours = approximately $13,600.

(3) 100 burden hours at a cost of $31,000[511] per large private equity fund adviser for the initial annual report;

(4) 50 burden hours at a cost of $13,900[512] per large private equity fund adviser for each subsequent annual report;

(5) 300 burden hours at a cost of $93,100[513] per large hedge fund adviser for the initial quarterly report;

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510 We expect that for subsequent reports senior personnel will bear less of the reporting burden. As a result, we estimate that these activities will most likely be performed equally by a compliance manager at a cost of $273 per hour, a senior compliance examiner at a cost of $235 per hour, a senior risk management specialist at a cost of $409 per hour and a risk management specialist at a cost of $192 per hour. ($273/hour x 0.25 + $235/hour x 0.25 + $409/hour x 0.25 + $192/hour x 0.25) x 15 hours = approximately $4,200.

511 The SEC expects that for the initial report, of a total estimated burden of 100 hours, approximately 60 hours will most likely be performed by compliance professionals and 40 hours will most likely be performed by programmers working on system configuration and reporting automation. Of the work performed by compliance professionals, the SEC anticipates that it will be performed equally by a compliance manager at a cost of $273 per hour and a senior risk management specialist at a cost of $409 per hour. Of the work performed by programmers, the SEC anticipates that it will be performed equally by a senior programmer at a cost of $304 per hour and a programmer analyst at a cost of $224 per hour. ($273/hour x 0.5 + $409/hour x 0.5) x 60 hours + ($304/hour x 0.5 + $224/hour x 0.5) x 40 hours = approximately $31,000.

512 The SEC expects that for subsequent reports senior personnel will bear less of the reporting burden and that significant system configuration and reporting automation costs will not be incurred. As a result, the SEC estimates that these activities will most likely be performed equally by a compliance manager at a cost of $273 per hour, a senior compliance examiner at a cost of $235 per hour, a senior risk management specialist at a cost of $409 per hour and a risk management specialist at a cost of $192 per hour. ($273/hour x 0.25 + $235/hour x 0.25 + $409/hour x 0.25 + $192/hour x 0.25) x 50 hours = approximately $13,900.

513 We expect that for the initial report, of a total estimated burden of 300 hours, approximately 180 hours will most likely be performed by compliance professionals and 120 hours will most likely be performed by programmers working on system configuration and reporting automation. Of the work performed by compliance professionals, we anticipate that it will be performed equally by a compliance manager at a cost of $273 per hour and a senior risk management specialist at a cost of $409 per hour. Of the work performed by programmers, we anticipate that it will be performed equally by a senior programmer at a cost of $304 per hour and a programmer analyst at a

(6) 140 burden hours at a cost of $38,800[514] per large hedge fund adviser for each subsequent quarterly report;

(7) 140 burden hours at a cost of $43,500[515] per large liquidity fund adviser for the initial quarterly report; and

(8) 65 burden hours at a cost of $18,000[516] per large liquidity fund adviser for each subsequent quarterly report.

Assuming that there are 3,070 smaller private fund advisers, 250 large hedge fund advisers, 80 large liquidity fund advisers, and 170 large private equity fund advisers, the

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cost of $224 per hour. ($273/hour x 0.5 + $409/hour x 0.5) x 180 hours + ($304/hour x 0.5 + $224/hour x 0.5) x 120 hours = approximately $93,100.

514 We expect that for subsequent reports senior personnel will bear less of the reporting burden and that significant system configuration and reporting automation costs will not be incurred. As a result, we estimate that these activities will most likely be performed equally by a compliance manager at a cost of $273 per hour, a senior compliance examiner at a cost of $235 per hour, a senior risk management specialist at a cost of $409 per hour and a risk management specialist at a cost of $192 per hour. ($273/hour x 0.25 + $235/hour x 0.25 + $409/hour x 0.25 + $192/hour x 0.25) x 140 hours = approximately $38,800.

515 The SEC expects that for the initial report, of a total estimated burden of 140 hours, approximately 85 hours will most likely be performed by compliance professionals and 55 hours will most likely be performed by programmers working on system configuration and reporting automation. Of the work performed by compliance professionals, the SEC anticipates that it will be performed equally by a compliance manager at a cost of $273 per hour and a senior risk management specialist at a cost of $409 per hour. Of the work performed by programmers, the SEC anticipates that it will be performed equally by a senior programmer at a cost of $304 per hour and a programmer analyst at a cost of $224 per hour. ($273/hour x 0.5 + $409/hour x 0.5) x 85 hours + ($304/hour x 0.5 + $224/hour x 0.5) x 55 hours = approximately $43,500.

516 The SEC expects that for subsequent reports senior personnel will bear less of the reporting burden and that significant system configuration and reporting automation costs will not be incurred. As a result, the SEC estimates that these activities will most likely be performed equally by a compliance manager at a cost of $273 per hour, a senior compliance examiner at a cost of $235 per hour, a senior risk management specialist at a cost of $409 per hour and a risk management specialist at a cost of $192 per hour. ($273/hour x 0.25 + $235/hour x 0.25 + $409/hour x 0.25 + $192/hour x 0.25) x 65 hours = approximately $18,000.

foregoing estimates suggest an annual cost of $107,000,000[517] for all private fund advisers in the first year of reporting and an annual cost of $59,800,000 in subsequent years.[518]

The cost estimates above assume that risk and compliance personnel (and, in the case of Large Private Fund Advisers filing an initial report, programmers) will carry out the work of reporting on Form PF. Some commenters suggested that employees in portfolio management as well as legal, controller and other back office functions may also be involved in compiling, reviewing and filing Form PF.[519] These commenters did not provide estimates for how the reporting burdens would be allocated among these groups of employees, and we believe the allocation is likely to vary significantly among advisers depending on the size and complexity of their operations. Based on available wage data, we do not believe that variations in the allocation of these responsibilities among the functions that we and commenters identified would result in significantly different aggregate cost estimates.[520]

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517 (3,070 smaller private fund advisers x $13,600 per initial annual report) + (170 large private equity fund advisers x $31,000 per initial annual report) + (250 large hedge fund advisers x $93,100 per initial quarterly report) + (250 large hedge fund advisers x 3 quarterly reports x $38,800 per subsequent quarterly report) + (80 large liquidity fund advisers x $43,500 per initial quarterly report) + (80 large liquidity fund advisers x 3 quarterly reports x $18,000 per subsequent quarterly report) = approximately $107,000,000.

518 (3,070 smaller private fund advisers x $4,200 per subsequent annual report) + (170 large private equity fund advisers x $13,900 per subsequent annual report) + (250 large hedge fund advisers x 4 quarterly reports x $38,800 per subsequent quarterly report) + (80 large liquidity fund advisers x 4 quarterly reports x $18,000 per subsequent quarterly report) = approximately $59,800,000.

519 *See, e.g.*, Kleinberg General Letter; MFA Letter.

520 For example, our estimates assume that the work is performed by compliance managers at $273 per hour, senior compliance examiners at $235 per hour, senior risk management

In addition, as discussed above, a private fund adviser must file very limited information on Form PF if it needs to transition from quarterly to annual filing, if it is no longer subject to the reporting requirements of Form PF or if it requires a temporary hardship exemption under rule 204(b)-1(f). We estimate that transition and final filings will, collectively, cost private fund advisers as a whole approximately $5,200 per year.[521] We further estimate that hardship exemption requests will cost private fund advisers as a whole approximately $760 per year.[522] No commenters addressed these estimates. The estimate with respect to hardship exemptions is unchanged from the proposal. The estimate with respect to transition and final filings have been reduced because fewer

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specialists at $409 per hour, risk management specialists at $192 per hour and, in the case of Large Private Fund Advisers filing an initial report, programmers ranging from $304 to $224 per hour. Based on the SIFMA Earnings Reports, indicative costs in the other functions that commenters identified are: $287 per hour for a senior portfolio manager; $211 per hour for an intermediate portfolio manager; $430 per hour for an assistant general counsel; $165 per hour for a fund senior accountant; $194 per hour for an intermediate business analyst; and $154 per hour for an operations specialist. An adviser's chief compliance officer (at a cost of $423 per hour) or controller (at a cost of $433 per hour) may also review the filing, though we would expect that in most cases their involvement would be more limited than that of more junior employees.

521 The SEC estimates that, for the purposes of the PRA, transition filings will impose 7 burden hours per year on private fund advisers in the aggregate and that final filings will impose 71 burden hours per year on private fund advisers in the aggregate. The SEC anticipates that this work will most likely be performed by a compliance clerk at a cost of $67 per hour. (7 burden hours + 71 burden hours) x $67/hour = approximately $5,200.

522 The SEC estimates that, for the purposes of the PRA, requests for temporary hardship exemptions will impose 4 burden hours per year on private fund advisers in the aggregate. The SEC anticipants that five-eighths of this work will most likely be performed by a compliance manager at a cost of $273 per hour and that three-eighths of this work will most likely be performed by a general clerk at a cost of $50 per hour. (($273 per hour x 5/8 of an hour) + ($50 per hour x 3/8 of an hour)) x 4 hours = approximately $760.

filers will be required to report on a quarterly basis and the addition of a minimum reporting threshold means that fewer advisers will report in total.[523]

Advisers may also incur costs related to the modification or deployment of systems to support their reporting obligations under Form PF.[524] As discussed above, certain of the anticipated costs to Large Private Fund Advisers of automating Form PF reporting are accounted for in our cost estimates.[525] In addition, Large Private Fund Advisers may incur costs associated with the acquisition or use of hardware needed to perform computations or otherwise process the data required on Form PF.[526] Commenters did not provide estimates for these costs. However, as discussed above, we estimate that these costs, which are likely to vary significantly among advisers, will range from $0 to $25,000,000 in the aggregate for the first year of reporting, with the actual costs likely to fall in between these two end-points.[527]

Based on the foregoing estimates, we estimate that the aggregate annual costs of Form PF, other than for hardware costs, are approximately $108,000,000 in the first year

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523 *See supra* note 424.

524 *See supra* section IV.G of this Release.

525 *See supra* note 438 and accompanying text.

526 *See supra* notes 434-441 and accompanying text.

527 *Id.*

and $60,500,000 in subsequent years.[528] In addition, we estimate that hardware costs will add between $0 and $25,000,000 in the first year.[529]

Reporting requirements can also impose costs beyond the direct costs associated with compiling and submitting data, and advisers subject to the Form PF reporting requirements may incur costs that are more difficult to quantify. One commenter, for instance, suggested an adviser may incur indirect "costs associated with the risk of disclosure of highly sensitive proprietary information."[530] As discussed above, Form PF elicits non-public information about private funds and their trading strategies, the public disclosure of which could adversely affect the funds and their investors.[531] We are, however, working to establish controls designed to protect this sensitive information from improper or inadvertent disclosure and believe that the risk of such disclosure is low.[532] If an adviser's Form PF data were disclosed despite the controls intended to maintain its confidentiality, there is some risk that a competitor may be able to use an adviser's data to replicate the adviser's trading strategy or trade against the adviser, thereby potentially harming the profitability of the strategy to that adviser. However, because data on Form PF generally could not, on its own, be used to identify individual investment

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528 $107,000,000 (for periodic reporting in the first year) + $5,200 (for transition and final filings) + $760 (for hardship requests) + $684,000 (for filing fees) = approximately $108,000,000. $59,800,000 (for periodic reporting in subsequent years) + $5,200 (for transition and final filings) + $760 (for hardship requests) + $684,000 (for filing fees) = approximately $60,500,000.

529 *See supra* notes 440-441 and accompanying text.

530 CCMR Letter.

531 *See supra* section II.D of this Release.

532 *See supra* sections II.D and II.E of this Release.

positions, the ability of a competitor to use Form PF data in this manner is limited.[533] In addition, the deadlines for filing Form PF have, in most cases, been significantly extended from the proposal, meaning that the filings will generally contain less current, and therefore less sensitive, data.[534] In the very unlikely event that improper or inadvertent disclosures of Form PF data occurred frequently, the disclosures could discourage advisers from investing the time and other resources required to develop novel strategies, potentially reducing the range of options available to investors and inhibiting financial innovation.

We do not expect this rulemaking to have a significant negative effect on competition because the information generally will be non-public and similar types of SEC-registered advisers will have comparable burdens under the Form.[535] In addition, the SEC does not expect this rulemaking to have a significant negative effect on capital formation, again because the information collected generally will be non-public and, therefore, should not affect private fund advisers' ability to raise capital.

Although Form PF data generally will be non-public, Form PF will increase transparency to regulators.[536] As discussed above, this may result in a positive effect on capital formation because advisers may, as a result, assess more carefully the risks associated with particular investments and, in the aggregate, allocate capital to

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533 *See supra* note 343.

534 *See supra* notes 351 and 344 and accompanying text.

535 *See supra* section II.D of this Release for a discussion of confidentiality of Form PF data.

536 *See supra* section II.D of this Release for a discussion of confidentiality of Form PF data.

investments with a higher value to the economy as a whole.[537] However, this increased transparency could also have a negative effect on capital formation if it increases advisers' aversion to risk and, as a result, reduces investment in projects that may be risky but beneficial to the economy as a whole. To the extent that changes in investment allocations lead to reduced economic outcomes in the aggregate, Form PF reporting may result in a negative effect on capital available for investment.

The SEC also recognizes that the direct costs of completing and filing Form PF may reduce the amount of capital that funds have available for investment or, if the costs are passed on to fund investors, reduce the amount of capital investors have available for investment. This could, in turn, affect capital formation.[538] However, the direct costs of reporting on Form PF will, to some extent, only transfer capital from private fund advisers to other market participants, such as employees or service providers paid to complete the Form. Because private fund advisers may have different investment opportunities than these other market participants, this transfer may negatively affect aggregate economic outcomes. However, some of this transferred capital will be invested or spent and will not represent an aggregate loss to the economy. In addition, the direct

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537 *See supra* note 494 and accompanying text.

538 One commenter expressed concern regarding the possible effects of Form PF reporting on economic growth, investors, investment opportunities, companies, markets, market liquidity and tax revenue as well as "the cost in terms of jobs and capital." Issa Letter. This commenter suggested that these potential negative effects could flow from several sources, including: (1) the possibility that advisers will locate funds outside the United States as a result of, or to avoid, Form PF compliance costs or that these costs will be passed on to investors, causing them to seek investment opportunities outside the United States; and (2) the possibility that advisers will form fewer funds, slow the growth of their funds or shut down existing funds as a result of, or to avoid, Form PF compliance costs. We address these possible sources of indirect costs below.

costs of Form PF are, on average, small compared to other economic incentives that motivate private funds and their advisers to invest and grow.[539]

One commenter expressed concern that this rulemaking could cause advisers, private funds or investors to seek investment opportunities outside the U.S. as a result of, for instance, increased costs.[540] This rulemaking could impose costs on U.S. private fund advisers that non-U.S. private fund advisers would not bear unless they are subject to the Advisers Act and the Form PF reporting requirements. However, advisers generally would not be able to avoid these reporting obligations by simply organizing the fund in a third country because regulatory jurisdiction for Form PF does not depend solely on where the fund is formed.[541] In addition, as noted above, ESMA has proposed a reporting regime similar to Form PF for alternative investment fund managers subject to the EU Directive. If that regime is adopted, we understand most such alternative investment managers would bear reporting costs similar to those that Form PF imposes. Accordingly, we believe the competitive impact of this difference in operating costs will be limited. We also do not expect that private funds will, to any significant extent, seek to avoid these regulatory burdens by foregoing participation in the U.S. capital markets because of the depth and liquidity of these markets and the stability afforded by the legal structures in the U.S.

This commenter also suggested that some fund advisers may determine not to form a new private fund if the costs of Form PF outweigh the marginal benefits the

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539 *See infra* notes 545 and 548 and accompanying text.

540 *See* Issa Letter.

541 *See supra* note 134 and accompanying text.

adviser expects to obtain by forming the fund.[542] Reduced fund formation could diminish competition and the number of choices available to investors. The SEC does not, however, believe the cost of reporting on Form PF will have a substantial negative effect on fund formation. An adviser with no existing private funds considering whether to form its first fund is likely to face little or no costs as a result of Form PF because it is unlikely to leap past a Large Private Fund Adviser Threshold and may not even exceed the minimum reporting threshold of $150 million in private fund assets under management.[543] For an existing private fund adviser, forming a new private fund would increase the cost of reporting on Form PF, but the adviser would be able to leverage its experience and existing systems, making the incremental reporting more efficient than for an adviser first becoming subject to Form PF reporting requirements.[544] In the case of either an adviser newly managing private funds or an adviser with existing private funds, the SEC believes that Form PF reporting costs are unlikely to discourage the formation of many funds because the costs of either becoming subject to Form PF as a smaller private fund adviser or reporting incrementally more information on Form PF are small when compared to possible management and performance fees. For example, the SEC

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542 *See* Issa Letter.

543 According to HFI data, even among the top 25 hedge fund launches reported in 2010, the average fund size was approximately $750 million, and existing advisers launched the majority of those funds in any case. This data also shows that, out of 135 total hedge fund launches reported in 2010 exceeding $50 million, at least 110 of them raised under $300 million. HFI does not report in their annual global review hedge fund launches under $50 million. *See* HFI 2011 Global Review, *supra* note 493. *See also supra* sections IV.A and IV.G of this Release (discussing estimates of Form PF reporting costs for smaller private fund advisers).

544 In addition, in the case of large hedge fund advisers, the more detailed information they must file in section 2b of the Form only applies to qualifying hedge funds that have at least $500 million in net assets.

estimates that the cost to smaller private fund advisers of completing and filing Form PF will average less than $14,000 per initial annual filing and $5,000 per subsequent annual filing – or less than 0.01% of assets under management for the smallest adviser subject to Form PF reporting requirements – compared to annual management and performance fees that, at least among hedge fund advisers, average approximately 1.5% of assets under management and 20% of excess returns, respectively.[545]

In addition, this commenter expressed concern that the Large Private Fund Adviser thresholds may encourage some private fund advisers with assets under management near but below the thresholds to attempt to staunch growth in their funds, either by refusing to admit new investors or by managing the investments of the funds, to remain below the thresholds.[546] Similarly, this commenter suggested that some funds may even shut down to avoid Form PF reporting costs.[547] The SEC believes, however, that substantial economic incentives will likely counter such behavior, including private fund performance fees that incentivize the private fund adviser to continue advising its funds and maximize fund appreciation and return. For example, a hedge fund with an initial value of $1.5 billion that experiences a 1% excess return will net $3 million in performance fees, and a 1% growth in assets under management will net an additional $225,000 per year in management fees, compared to an estimated cost of between

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545 *See* Ibbotson, et al., *supra* note 95, at 15 (finding a management fee of 1.5% of assets under management and a 20% performance fee to be the median fee structure in the TASS hedge fund database). $14,000 / $150,000,000 = approximately 0.009%.

546 *See* Issa Letter.

547 *Id.*

$210,000 and $260,000 in the first year of reporting.[548] In addition, we believe the cost to an adviser of reporting will decline over time as the adviser becomes more familiar with the Form and realizes efficiencies while, at the same time, the adviser will continue to charge management fee and potentially collect performance fees each year. With respect to the large adviser threshold specifically, we anticipate that business relations with investors that may be damaged if the adviser turns away investor assets may also motivate advisers to continue to permit the size of their funds to increase as a result of new investment.

As discussed above, we believe that private fund advisers, investors in private funds and the companies in which private funds may invest will enjoy certain benefits related to Form PF.[549] We recognize, however, that many of Form PF's benefits will be widely distributed across the financial system while its costs will be concentrated. Private fund advisers will bear most of these costs, though they may also pass some of these costs on to fund investors, and to the extent that capital available for investment is reduced, the companies in which private funds would otherwise invest may also bear costs. In addition, the costs of Form PF to an individual adviser will vary depending on factors such as the state of its existing systems and the complexity of its business. As a result, the costs and benefits of Form PF to particular advisers, particular investors,

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548 The calculations assume a management fee of 1.5% of assets under management and a 20% performance fee. *See supra* note 545. $93,100 for the initial quarterly report + $38,800 for each subsequent quarterly reporting x 3 quarterly reports = approximately $210,000 for the first year of reporting. *See supra* notes 513-514. In addition, the SEC has estimated that a Large Private Fund Adviser may incur between $0 and $50,000 in costs for the acquisition or use of hardware in the first year of reporting. *See supra* note 441 and accompanying text.

549 *See supra* section V.A of this Release.

particular companies and individual American citizens will not be evenly distributed. For certain individuals and entities, the costs of Form PF may even exceed the benefits to them. However, we believe that the aggregate benefits of this rulemaking will be substantial. Moreover, the uneven distribution of the benefits and costs of Form PF reflects the potential for an uneven distribution of the costs and benefits of engaging in risky financial activities that may impose negative externalities.[550]

C. CFTC Statutory Findings

Rule 4.27, as finalized, would deem a CPO registered with the CFTC that is dually registered as a private fund adviser with the SEC to have satisfied certain reporting requirements that the CFTC may adopt by filing Form PF with the SEC. The CPOs and CTAs that are dually registered as private fund advisers would be required to provide annually a limited amount of basic information on Form PF about the operations of their private funds. Only large CPOs and CTAs that are also registered as private fund advisers with the SEC would have to submit on a quarterly basis the full complement of

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[550] *See, e.g.*, Iman Anabtawi and Steven L. Schwarcz, *Regulating Systemic Risk: Towards an Analytical Framework*, 86 NOTRE DAME L. REV. 4, 27 (2011) (arguing that financial market participants will not expend sufficient effort to identify and avoid conditions giving rise to systemic risk and explaining that one factor contributing to this behavior is that "the benefits of exploiting finite capital resources accrue to individual market participants, each of whom is motivated to maximize use of the resource, whereas the costs of exploitation are distributed more widely.... The root of the commons problem in financial markets is the asymmetry in the distribution of gains and losses associated with investment decisions.... In the case of a positive outcome, the firm captures the full benefits of the investment's success. In the case of a negative outcome, however, the firm may not suffer the full consequences of the poor investment. Rather, if the firm fails or merely defaults, those consequences will impact financial market participants that rely on the soundness of the firm's financial condition. Furthermore, if the firm is deemed too systemically significant to fail, its loss may be absorbed by government as a lender of last resort. In either case, the uninternalized costs associated with risk-taking by financial firms leads them to overexploit scarce capital resources in the form of socially excessive risk-taking.").

systemic risk related information required by Form PF.[551] As noted above, the Dodd-Frank Act tasks FSOC with monitoring the financial services marketplace in order to identify potential threats to the financial stability of the United States.[552] The Dodd-Frank Act also requires FSOC to collect information from member agencies – like the SEC and the CFTC – to support its functions.[553] The CFTC and the SEC are jointly adopting sections 1 and 2 of Form PF as a means to collect the information necessary to permit FSOC to fulfill its obligation to monitor private funds, and in order to identify any potential systemic threats arising from their activities. The CFTC and the SEC do not currently collect the information that is covered in proposed sections 1 and 2 of Form PF.

Section 15(a) of the CEA requires that the CFTC, before promulgating a regulation under the Act or issuing an order, consider the costs and benefits of its action. By its terms, CEA Section 15(a) does not require the CFTC to quantify the costs and benefits of a new regulation or determine whether the benefits of the regulation outweigh its costs. Rather, CEA section 15(a) simply requires the CFTC to "consider the costs and benefits" of its action. CEA section 15(a)(2) specifies that costs and benefits shall be evaluated in light of the following considerations: (1) protection of market participants and the public; (2) efficiency, competitiveness and financial integrity of futures markets; (3) price discovery; (4) sound risk management practices; and (5) other public interest considerations.[554] Accordingly, the CFTC could, in its discretion, give greater weight to

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551 See 5 U.S.C. 801(a)(1)(B)(i).

552 See section 112(a)(2)(C) of the Dodd-Frank Act.

553 See section 112(d)(1) of the Dodd-Frank Act.

554 7 U.S.C. 19(a).

any of the five considerations and could, in its discretion, determine that, notwithstanding its costs, a particular regulation was necessary or appropriate to protect the public interest or to effectuate any of the provisions or to accomplish any of the purposes of the Act.

Before promulgating these final rules, the CFTC sought public comment on the rules themselves, including the cost-benefit considerations of section 1 and 2 of Form PF.[555] The CFTC also specifically invited commenters to submit "any data or other information that they may have quantifying or qualifying the perceived costs and benefits of this proposed rule with their comment letters."[556] As noted above, the CFTC and the SEC received comments on the cost and benefits of the proposed regulations and the estimates of costs included in the Proposing Release, and they have carefully considered those comments. CEA Rule 4.27 does not impose any additional burdens or costs upon registered CPOs and CTAs that are dually registered as investment advisers with the SEC. By filing Form PF with the SEC, these dual registrants would be deemed to have satisfied certain reporting obligations with the CFTC, should the CFTC adopt such requirements.

1. General Costs and Benefits

With respect to costs, the CFTC has determined that: (1) without the reporting requirements imposed by this rulemaking, FSOC will not have sufficient information to identify and address potential threats to the financial stability of the United States (such as the near collapse of Long Term Capital Management); (2) the reporting requirements,

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555 *See generally*, CFTC Proposing Release, *supra* note 16, at 76 FR 8068, 8087 (for CFTC's request for comment on the cost-benefit considerations).

556 *See generally*, CFTC Proposing Release, *supra* note 16, at 76 FR 8068, 8087.

once finalized, will provide the CFTC with better information regarding the business operations, creditworthiness, use of leverage, and other material information of certain registered CPOs and CTAs that are also registered as investment advisers with the SEC; and (3) while they are necessary to U.S. financial stability, the reporting requirements will create additional compliance costs for these registrants, as discussed in the foregoing portions of the Economic Analysis as well as in the PRA section of this Release.

The CFTC has determined that the proposed reporting requirements will provide a benefit to all investors and market participants by providing the CFTC and other policy makers with more complete information about these registrants and the potential risk their activities may pose to the U.S. financial system. In turn, this information will enhance the CFTC's ability to appropriately tailor its regulatory policies to the commodity pool industry and its operators and advisors. As mentioned above, the CFTC and the SEC do not have access to this information today and have instead been made to use information from other, less reliable sources.

2. Section 15(a) Determination

As stated above, section 15(a) of the CEA requires the CFTC to consider the costs and benefits of its actions in light of five broad areas of market and public concern: (1) protection of market participants and the public; (2) efficiency, competitiveness, and financial integrity of futures markets; (3) price discovery; (4) sound risk management practices; and (5) other public interest considerations.

a. Protection of Market Participants and the Public

Should the CFTC adopt certain of its proposed systemic risk reporting requirements, the coordination between the CFTC and SEC on this rulemaking would

result in significant efficiencies for any private fund adviser that is also registered as a CPO or CTA with the CFTC. This is because, under CEA rule 4.27, filling Form PF would satisfy both SEC and CFTC reporting obligations with respect to commodity pools that are "private funds" and may satisfy CFTC reporting obligations with respect to commodity pools that are not "private funds," in each case should the CFTC adopt such reporting obligations. As noted above, the CFTC has determined that this coordination will protect such participants from duplicative reporting while still providing FSOC with needed information to fulfill its mission to protect the public from potential threats to the financial stability of the United States.

Commodity pools that fall within the definition of private funds and will be filing Form PF represent a sector of collective investment vehicles that have experienced a substantial growth and have been the subject of international concern regarding their size in juxtaposition with the markets as a whole. This concern has led to several countries instituting similar data collection efforts and it is well recognized that the U.S. contingent of these funds represents a sizable portion of all trading by this type of entity. Thus, this combined SEC/CFTC effort will contribute substantially to a better understanding of the impact of private investment vehicles on both the U.S. and international markets and provide the information necessary to intelligently develop regulatory efforts and oversight programs to provide adequate protection of market participants and the public at large.

Finally, the CFTC agrees with the SEC that Form PF, as adopted, will increase the amount and quality of information available regarding a previously opaque area of

investment activity and, thereby, enhance the ability of regulators to protect investors and oversee the markets that they regulate.

b. Efficiency, Competitiveness, and Financial Integrity of Futures Markets

Although the CFTC does not believe this rule relates directly to the efficiency or competitiveness of futures markets, the CFTC does recognize that the interconnectedness of the United States financial system is such that the integrity of futures markets depends on the financial stability of the entire financial system. To the extent that the information collected by Form PF assists the Commissions and FSOC to identify threats that may damage the United States financial system, the regulations herein indirectly protect the integrity of futures markets.

c. Price Discovery

The CFTC has not identified a specific effect on price discovery as a result of Form PF or related regulations.

d. Sound Risk Management

The Dodd-Frank Act tasks FSOC and its member agencies (including both the SEC and the CFTC) with mitigating risks to the financial stability the United States. The CFTC believes these regulations are necessary to fulfill that obligation. Risk management is provided by these regulations in two main ways: (1) assisting FSOC in fulfilling its mission of protecting the systemic financial stability of the United States; and (2) improving the ability of regulators to oversee markets. These benefits are shared by market participants, at least indirectly, as a part of the United States financial system. In addition, CPOs and CTAs that are dually registered as investment advisers will benefit

from these regulations to the extent that reporting on Form PF requires such entities to review their firms' portfolios, trading practices, and risk profiles; thus, the CFTC believes that these regulations may improve the sound risk management practices within their internal risk management systems.

e. Other Public Interest Considerations

The CFTC has not identified other public interest considerations related to the costs and benefits of these regulations.

VI. FINAL REGULATORY FLEXIBILITY ANALYSIS

SEC:

The SEC has prepared the following Final Regulatory Flexibility Analysis ("FRFA") regarding Advisers Act rule 204(b)-1 in accordance with section 4(a) of the Regulatory Flexibility Act ("RFA").[557] The SEC prepared the Initial Regulatory Flexibility Analysis ("IRFA") in conjunction with the Proposing Release in January 2011.[558]

A. Need for and Objectives of the New Rule

New Advisers Act rule 204(b)-1 and Form PF implement provisions of the Dodd-Frank Act by specifying information that private fund advisers must disclose confidentially to the SEC, which information the SEC will provide to FSOC for systemic risk assessment purposes. Under the new rule, private fund advisers must file information responsive to all or portions of Form PF on a periodic basis. The scope of the required information and the frequency of the reporting is related to the amount of

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557 5 U.S.C. 603(a).

558 *See* Proposing Release, *supra* note 12, at section VI.

private fund assets that each private fund adviser manages and the type of private fund to which those assets relate. Specifically, smaller private fund advisers and large private equity advisers must report annually, while large hedge fund and liquidity fund advisers must report quarterly and provide additional information regarding the hedge funds and liquidity funds, respectively, that they manage.[559]

B. Significant Issues Raised by Public Comment

In the Proposing Release, we requested comment on the IRFA. In particular, we sought comment on the number of small entities, particularly small advisers, to which the new Advisers Act rule and reporting requirements would apply and the effect on those entities, including whether the effects would be economically significant. None of the comment letters we received addressed the IRFA or the effect of the proposal on small entities, as that term was used in the IRFA.

C. Small Entities Subject to the Rule

Under SEC rules, for the purposes of the Advisers Act and the Regulatory Flexibility Act, an investment adviser generally is a small entity if it: (i) has assets under management having a total value of less than $25 million; (ii) did not have total assets of $5 million or more on the last day of its most recent fiscal year; and (iii) does not control, is not controlled by, and is not under common control with another investment adviser that has assets under management of $25 million or more, or any person (other than a

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559 *See* section II.A of this Release (describing who must file Form PF), section II.B of this Release (discussing the frequency with which private fund advisers must file Form PF), and section II.C of this Release (describing the information that private fund advisers must report on Form PF). *See also* proposed Instruction 9 to Form PF for information regarding the frequency with which private fund advisers must file Form PF.

natural person) that had total assets of $5 million or more on the last day of its most recent fiscal year.[560]

Advisers Act rule 204(b)-1 requires an investment adviser registered with the SEC to file certain information on Form PF if it manages one or more private funds and had at least $150 million in regulatory assets under management attributable to private funds as of the end of its most recently completed fiscal year. Under section 203A of the Advisers Act, most advisers qualifying as small entities are prohibited from registering with the SEC and are instead registered with state regulators. Therefore, few small advisers will meet the registration criterion. Fewer still are likely to meet the minimum reporting threshold of $150 million in regulatory assets under management attributable to private funds. By definition, no small entities will, on their own, meet this threshold, which the SEC did not include in the proposal but has added in response to commenter concerns.[561] Advisers are, however, required to determine whether they exceed this threshold by aggregating their private fund assets under management with those of their related persons (other than separately operated related persons), with the result that some small entities may be subject to Form PF reporting requirements.[562] The SEC does not have a precise count of the number of advisers that may satisfy the minimum reporting

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560 *See* Advisers Act rule 0-7(a).

561 *See supra* note 56-59 and accompanying text.

562 *See supra* section II.A.5 of this Release. The SEC notes that related persons are permitted to file on a single Form PF. As a result, even in the case that a larger related person causes a small entity to exceed the minimum reporting threshold, the small entity may not ultimately bear the reporting burden. *See supra* section II.A.6 of this Release. In addition, under Advisers Act rule 0-7(a)(3), an adviser with affiliates exceeding the other small entity thresholds under that rule would not be regarded as a small entity, suggesting that it may not be possible both to qualify as a small entity under that rule and to satisfy the criteria that would subject an adviser to Form PF reporting obligations.

threshold based on the aggregate private fund assets that it and its related persons manage because such advisers file separate reports on Form ADV. However, because of the new minimum reporting threshold, the group of small entities subject to the rule as adopted will be a subset of the group that would have been subject to the proposed rule. In the Proposing Release, the SEC estimated that approximately 50 small entities were registered with the SEC and advised one or more private funds.[563] Accordingly, the SEC estimates that no more than 50 small entities are likely to become subject to Form PF reporting obligations under the final rule.

D. Projected Reporting, Recordkeeping and other Compliance Requirements

Advisers Act rule 204(b)-1 and Form PF impose certain reporting and compliance requirements on advisers, including small advisers. A small adviser that is subject to the rule must complete all or part of section 1 of the Form. As discussed above, the SEC estimates that completing, reviewing and filing Form PF will cost approximately $13,600 for each small adviser in its first year of reporting and $4,200 per year for each subsequent year.[564] In addition, small entities must pay a filing fee of $150 per annual filing.[565]

E. Agency Action to Minimize Effect on Small Entities

The Regulatory Flexibility Act directs the SEC to consider significant alternatives that would accomplish the stated objective, while minimizing any significant impact on

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563 *See* Proposing Release, *supra* note 12, at n.212 and accompanying text.

564 *See supra* notes 509-510 and accompanying text.

565 *See supra* note 432 and accompanying text.

small entities. In connection with the proposed rules and amendments, the SEC considered the following alternatives: (1) the establishment of differing compliance or reporting requirements or timetables that take into account the resources available to small entities; (2) the clarification, consolidation, or simplification of compliance and reporting requirements under the rule for small entities; (3) the use of performance rather than design standards; and (4) an exemption from coverage of the rule, or any part thereof, for small entities.

Regarding the first and fourth alternatives, the SEC is adopting a minimum reporting threshold of $150 million as well as reporting requirements and timetables that differ for entities of smaller sizes. A small entity adviser that is subject to the rule only needs to file Form PF annually and complete applicable portions of section 1 of the form.[566] Large Private Fund Advisers must file additional information, and large hedge fund or large liquidity fund advisers must file more frequently. In addition, the filing fees that a smaller adviser must pay in a given year are lower than those that a large hedge fund or large liquidity fund advisers must pay over the same period. Regarding the second alternative, the information that a small entity subject to the rule must provide under section 1 of Form PF is much simpler than the information required of large hedge fund or large liquidity fund advisers and is consolidated in one section of the form. Regarding the third alternative, the SEC has, in a number of cases, permitted advisers to rely on their own methodologies in providing the information that the Form requires,

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[566] If the adviser has no hedge fund assets under management, it need not complete section 1.C of the Form. Advisers that manage a significant amount of both registered money market fund and liquidity fund assets must complete section 3 of Form PF, but there are no small entities that manage a registered money market fund.

though the use of performance standards is limited by the need to obtain comparable information from all filers.

CFTC:

Under CEA rule 4.27, the CFTC would not impose any additional burden upon registered CPOs and CTAs that are dually registered as investment advisers with the SEC because such entities are only required to file Form PF with the SEC. Further, certain CPOs registered with the CFTC that are also registered with the SEC would be deemed to have satisfied certain CFTC-related filing requirements, should the CFTC adopt such requirements, by completing and filing the applicable sections of Form PF with the SEC. Therefore, any burden imposed by Form PF through rule 4.27 on small entities registered with both the CFTC and the SEC has been accounted for within the SEC's calculations regarding the impact of this collection of information under the RFA or, to the extent the reporting may relate to commodity pools that are not private funds, the CFTC anticipates that it would account for this burden should it adopt a future rulemaking establishing reporting requirements with respect to those commodity pools. Accordingly, the Chairman, on behalf of the CFTC, hereby certifies pursuant to 5 U.S.C. 605(b) that the rules as adopted will not have a significant impact on a substantial number of small entities.

VII. STATUTORY AUTHORITY

CFTC:

The CFTC is adopting rule 4.27 [17 CFR 4.27] pursuant to its authority set forth in section 4n of the Commodity Exchange Act [7 U.S.C. 6n].

SEC:

The SEC is adopting rule 204(b)-1 [17 CFR 275.204(b)-1] pursuant to its authority set forth in sections 204(b) and 211(e) of the Advisers Act [15 U.S.C. 80b-4 and 15 U.S.C. 80b-11], respectively.

The SEC is adopting rule 279.9 pursuant to its authority set forth in sections 204(b) and 211(e) of the Advisers Act [15 U.S.C. 80b-4 and 15 U.S.C. 80b-11], respectively.

LIST OF SUBJECTS

17 CFR Part 4

Advertising, Brokers, Commodity futures, Commodity pool operators, Commodity trading advisors, Consumer protection, Reporting and recordkeeping requirements.

17 CFR Parts 275 and 279

Reporting and recordkeeping requirements, Securities.

TEXT OF FINAL RULES

Commodity Futures Trading Commission

For the reasons set out in the preamble, the CFTC is amending Title 17, Chapter I of the Code of Federal Regulations as follows:

PART 4—COMMODITY POOL OPERATORS AND COMMODITY TRADING ADVISORS

1. The authority citation for part 4 continues to read as follows:

Authority: 7 U.S.C. 1a, 2, 4, 6(c), 6b, 6c, 6l, 6m, 6n, 6o, 12a, and 23.

* * * * *

2. Add §4.27 to read as follows:

§4.27 Additional reporting by advisors of commodity pools.

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Investment advisers to private funds. Except as otherwise expressly provided in this section, CPOs and CTAs that are dually registered with the Securities and Exchange Commission and are required to file Form PF pursuant to the rules promulgated under the Investment Advisers Act of 1940, shall file Form PF with the Securities and Exchange Commission in lieu of filing such other reports with respect to private funds as may be required under this section. In addition, except as otherwise expressly provided in this section, CPOs and CTAs that are dually registered with the Securities and Exchange Commission and are required to file Form PF pursuant to the rules promulgated under the Investment Advisers Act of 1940, may file Form PF with the Securities and Exchange Commission in lieu of filing such other reports with respect to commodity pools that are not private funds as may be required under this section. Dually registered CPOs and CTAs that file Form PF with the Securities and Exchange Commission will be deemed to have filed Form PF with the Commission for purposes of any enforcement action regarding any false or misleading statement of a material fact in Form PF.

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Securities and Exchange Commission

For the reasons set out in the preamble, the SEC is amending Title 17, Chapter II of the Code of Federal Regulations as follows:

PART 275 – RULES AND REGULATIONS, INVESTMENT ADVISERS ACT OF 1940

3. The authority citation for Part 275 continues to read in part as follows:

Authority: 15 U.S.C. 80b-2(a)(11)(G), 80b-2(a)(17), 80b-3, 80b-4, 80b-4a, 80b-6(4), 80b-6a, and 80b-11, unless otherwise noted.

* * * * *

4. Section 275.204(b)-1 is added to read as follows:

§ 275.204(b)-1 Reporting by investment advisers to private funds.

(a) *Reporting by investment advisers to private funds on Form PF*. If you are an investment adviser registered or required to be registered under section 203 of the Act (15 U.S.C. 80b-3), you act as an investment adviser to one or more private funds and, as of the end of your most recently completed fiscal year, you managed private fund assets of at least $150 million, you must complete and file a report on Form PF (17 CFR 279.9) by following the instructions in the Form, which specify the information that an investment adviser must provide. Your initial report on Form PF is due no later than the last day on which your next update would be timely in accordance with paragraph (e) if you had previously filed the Form; provided that you are not required to file Form PF with respect to any fiscal quarter or fiscal year ending prior to the date on which your registration becomes effective.

(b) *Electronic filing*. You must file Form PF electronically with the Form PF filing system on the Investment Adviser Registration Depository (IARD).

Note to paragraph (b): Information on how to file Form PF is available on the Commission's website at http://www.sec.gov/iard.

(c) *When filed*. Each Form PF is considered filed with the Commission upon acceptance by the Form PF filing system.

(d) *Filing fees*. You must pay the operator of the Form PF filing system a filing fee as required by the instructions to Form PF. The Commission has approved the amount of the filing fee. No portion of the filing fee is refundable. Your completed Form PF will not be accepted by the operator of the Form PF filing system, and thus will not be considered filed with the Commission, until you have paid the filing fee.

(e) *Updates to Form PF*. You must file an updated Form PF:

(1) At least annually, no later than the date specified in the instructions to Form PF; and

(2) More frequently, if required by the instructions to Form PF. You must file all updated reports electronically with the Form PF filing system.

(f) *Temporary hardship exemption.*

(1) If you have unanticipated technical difficulties that prevent you from submitting Form PF on a timely basis through the Form PF filing system, you may request a temporary hardship exemption from the requirements of this section to file electronically.

(2) To request a temporary hardship exemption, you must:

(i) Complete and file in paper format, in accordance with the instructions to Form PF, Item A of Section 1a and Section 5 of Form PF, checking the box in Section 1a indicating that you are requesting a temporary hardship exemption, no later than one business day after the electronic Form PF filing was due; and

(ii) Submit the filing that is the subject of the Form PF paper filing in electronic format with the Form PF filing system no later than seven business days after the filing was due.

(3) The temporary hardship exemption will be granted when you file Item A of Section 1a and Section 5 of Form PF, checking the box in Section 1a indicating that you are requesting a temporary hardship exemption.

(4) The hardship exemptions available under § 275.203-3 do not apply to Form PF.

(g) *Definitions*. For purposes of this section:

(1) *Assets under management* means the regulatory assets under management as determined under Item 5.F of Form ADV (§ 279.1 of this chapter).

(2) *Private fund assets* means the investment adviser's assets under management attributable to private funds.

PART 279 – FORMS PRESCRIBED UNDER THE INVESTMENT ADVISERS ACT OF 1940

5. The authority citation for Part 279 continues to read as follows:

Authority: 15 U.S.C. 80b-1, *et seq*.

6. Section 279.9 is amended to read as follows:

§ 279.9 Form PF, reporting by investment advisers to private funds.

This form shall be filed pursuant to Rule 204(b)-1 (§ 275.204(b)-1 of this chapter) by certain investment advisers registered or required to register under section 203 of the Act (15 U.S.C. 80b-3) that act as an investment adviser to one or more private funds.

Note: The text of the following Form PF will not appear in the Code of Federal Regulations.

[**Insert Form PF**]

By the Commodity Futures Trading Commission.

David A. Stawick
Secretary

Date: October 31, 2011

By the Securities and Exchange Commission.

Elizabeth M. Murphy
Secretary

Date: October 31, 2011