January 28, 2011

By Mail and Electronic Delivery

The Honorable Mary L. Schapiro
Chairman
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

Re: File No. S7-36-10; Rel. No. IA-3110
Rules Implementing Amendments to the Investment Advisers Act of 1940

File No. S7-37-10; Rel. No. IA-3111
Exemptions for Advisers to Venture Capital Funds, Private Fund Advisers With Less Than $150 Million in Assets Under Management, and Foreign Private Advisers

Dear Chairman Schapiro:

The Coalition of Private Investment Companies ("CPIC")[1] is pleased to submit this letter to the Securities and Exchange Commission ("Commission") on the above-referenced proposals relating to the registration and regulation of advisers to certain private investment funds. We appreciate the Commission's efforts to implement reforms as required by the Dodd-Frank Wall Street Reform and Consumer Protection Act ("DFA"), especially in light of the large numbers of rulemakings and the tight deadlines that DFA requires.

CPIC strongly supported legislation to require registration of advisers to private investment funds.[2] We also supported legislation to give the Commission authority to obtain, and share with other regulators, information from advisers necessary and appropriate for the protection of investors and the assessment of systemic risk. We have further supported requiring private investment funds to provide basic census data in an online, publicly available form.[3]

[1] CPIC is a coalition of private investment companies who are diverse in size and in the investment strategies they pursue. Established in 2005, CPIC informs policy-makers, the media and the public about the private fund industry and its role in the capital markets.

[2] *See* Testimony of James Chanos, Chairman, CPIC before the House of Representatives Financial Services Committee: Hearing on Regulating Hedge Funds and Other Private Investment Pools (Oct. 6, 2009) (*available at* http://financialservices.house.gov/media/file/hearings/111/chanos_testimony.pdf).

[3] *Id.*

Title IV of the DFA amended the Investment Advisers Act of 1940 ("Advisers Act") to require registration of most private investment fund advisers and to authorize the Commission to provide a limited reporting regime for certain others. While Title IV did not specify new public disclosure requirements for registered investment advisers, including private fund advisers, CPIC has long supported proposals for more transparency for private investment funds and therefore generally supports the Commission's proposal to expand the information available on Form ADV for investment advisers to private funds.

We note, however, that the Commission recently proposed rules to implement new Subsection 204(b) of the Advisers Act, which authorizes the Commission to require private investment funds to maintain records and provide reports to the Commission in a number of areas for the Financial Stability Oversight Council's ("FSOC's") assessment of systemic risk or for the protection of investors and the public interest.[4] Recognizing the sensitivity of information such as trading positions and similar information that would reveal private funds' proprietary strategies, new Subsection 204(b) of the Advisers Act sets forth significant protections for confidential, proprietary information that relates to private investment funds and their advisers. We believe the dichotomy between investor-relevant information versus other information which, because of its confidential and propriety nature, should be available only to regulators is one that the Commission should continue to observe as it develops private fund investment adviser reporting requirements.

I. CPIC Supports the Proposals to Implement an Enhanced Disclosure Scheme for Investment Advisers to Private Funds.

DFA made fundamental changes to the current federal-state scheme of registration for investment advisers. In brief, Section 410 of the DFA amended Section 203A of the Advisers Act to delegate general responsibility for the registration and regulation of "Mid-Sized Investment Advisers" (those with between $25 and $100 million in assets under management ("AUM")) to the States. Under the revisions to the Advisers Act, and the Commission's proposed rules, advisers with $100 million or more in AUM will have to register with the Commission.[5] Mid-sized advisers will not be permitted to register with the Commission if they are required to register and are subject to examination by the State authorities where they maintain their principal office and place of business. On the other

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[4] *See Reporting by Investment Advisers to Private Funds and Certain Commodity Pool Operators and Commodity Trading Advisors on Form PF*, SEC Rel. No. IA-3145 (Jan. 26, 2011). Subsection 204(b) was added to the Advisers Act by Section 404 of the DFA. Under Section 406 of the DFA, the Commission and the Commodity Futures Trading Commission ("CFTC") must jointly promulgate rules to establish the form and content of reports required to be filed with the Commission pursuant to new Subsection 204(b) and with the CFTC by advisers that are registered with both agencies.

[5] Also, as noted below, the Commission is proposing to define the terms of another voluntary "private fund adviser exemption" from registration for advisers with less than $150 million in AUM in the U.S. In general, the States would register advisers with smaller amounts of AUM.

hand, if an adviser is (a) not required to register in that State; (b) would not be subject to examination by that State regulator, or (c) would have to register in 15 or more States, then it could register with the Commission, unless some other exemption applies.[6]

For these purposes, and for purposes of determining other regulatory obligations and exemptions that are triggered by levels of AUM, the Commission also proposes to change how assets are to be counted.[7] Thus, calculation of AUM would include all assets for which an adviser provides continuous and regular supervisory or management services, including certain items that do not have to be counted under current standards, such as family assets, proprietary assets, assets where the adviser receives no compensation, assets of foreign clients, clients' outstanding indebtedness, and uncalled commitments of private funds. AUM would also include the value of any private fund over which an adviser exercises continuous and regulator supervisory or management services, regardless of the nature of the fund's assets.[8] Finally, advisers would be required to value assets at fair value for these purposes.[9]

While this undoubtedly will require the registration of more investment advisers over the $100 million threshold, the proposed rules specify three significant types of advisers that would remain unregistered. Thus, the Commission proposes a new definition of the term "venture capital fund" in order to implement a voluntary exemption from registration for advisers to such funds pursuant to new Section 203(l) of the Advisers Act.[10] In addition, the Commission proposes rules to define the terms of another voluntary "private fund adviser exemption" from registration for advisers with less than $150 million in AUM in the U.S. pursuant to new Section 203(m) of the Advisers Act.[11] However, both

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[6] *Rules Implementing Amendments to the Investment Advisers Act of 1940*, SEC Rel. No. IA-3110, 75 FR 77052 (Dec. 10, 2010). About 4,100 Commission-registered advisers must switch to State registration. 75 FR 77054.

[7] 75 FR 77055 - 77058.

[8] 75 FR 77056; Proposed Instruction 5.b.(1) to Form ADV.

[9] 75 FR 77057; Proposed Instruction 5.b.(4) to Form ADV.

[10] The Commission would define a venture capital fund as one that: (1) invests in equity securities of private companies in order to provide operating and business expansion capital (i.e., "qualifying portfolio companies") and at least 80 percent of each company's securities owned by the fund are acquired directly from the qualifying portfolio company; (2) directly, or through its investment advisers, offers or provides significant managerial assistance to, or controls, the portfolio company; (3) does not borrow or otherwise incur leverage (other than limited short-term borrowing); (4) does not offer its investors redemption or other similar liquidity rights except in extraordinary circumstances; (5) represents itself as a venture capital fund to investors; and (6) is not registered under the Investment Company Act and has not elected to be treated as a BDC. Proposed Rule 203(l)-1; 75 FR 77192.

[11] Specifically, under proposed new Rule 203(m)-1, an adviser would qualify for the exemption under the following conditions: (1) the adviser may only advise private funds (it may advise any number of funds, so long as their aggregate assets are less than $150 million); (2) the adviser must calculate AUM as of the end of each calendar quarter (sub-advisers would count only those assets for which they have responsibility). As to non-U.S. private fund managers, if the adviser's principal office and place of business are outside the U.S.,

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of these types of unregistered private fund advisers would be subject, to certain reporting requirements, noted below. Finally, the Commission proposes to adopt rules to define the terms of an exemption from registration for "foreign private advisers" added to the Advisers Act by DFA Section 403.[12]

CPIC believes these proposals are consistent with legislative direction. However, we have previously testified in favor of Commission registration of *all* advisers to private investment funds, no matter how styled, and regardless of class of entity, nature of assets, or strategy. This is because, no matter the type or size of the fund, certain risks of misconduct are present. As we noted in testimony before the House Financial Services Committee in October 2009:

> [W]e question whether a category of private funds should be relieved of SEC registration, record-keeping, and inspection solely by virtue of its asset class and operations. Indeed, Ponzi schemes and frauds can be run with any asset class, and the lines between different categories of private funds tend to blur over time. We believe the registration requirement should apply to all private funds, whether they are hedge funds, private equity funds, or venture capital funds.[13]

While the DFA established an alternative reporting regime for venture fund advisers, we believe the Commission may wish to consider supplementing its proposal to include measures that would provide additional protection of investors in venture capital funds similar to those provided to investors in hedge funds and private equity funds. For example, the Commission could require venture capital fund advisers and private fund advisers to disclose whether assets are held at an independent custodial bank, trust company or broker-dealer, since the Commission's current custody rules only apply to

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the exemption would remain available as long as: (a) all of its clients that are U.S. persons (as defined in Regulation S) must be private funds. (This allows the adviser to have non-U.S. individuals and U.S. private funds as clients, but does not permit it to have U.S. individuals as clients). In addition, such a non-U.S. adviser would only count private fund assets that it manages from a place of business in the U.S. toward the $150 million asset limit.

[12] In brief, the Commission proposes new Rule 202(a)(3)-1 to define a "foreign private adviser" as one that (a) has no place of business in the U.S.; (b) has, in total, fewer than 15 clients and investors in the U.S. in private funds advised by the adviser; (c) has aggregate assets under management attributable to clients in the United States and investors in the United States in private funds advised by the investment adviser of less than $25 million; and (d) does not hold itself out in the U.S. as an investment adviser. SEC Rel. No. IA-3111, 75 FR 77210.

[13] Testimony of James Chanos, Chairman, CPIC before the House of Representatives Financial Services Committee: Hearing on Regulating Hedge Funds and Other Private Investment Pools (Oct. 6, 2009) (available at http://financialservices.house.gov/media/file/hearings/111/chanos_testimony.pdf).

advisers that are registered or required to register. [14] Small private funds are just as likely to be used as vehicles for Ponzi schemes as large funds. Indeed, many, if not most, Ponzi schemes involve managers with less than $150 million under management. Nor is a fund less susceptible to the risk of theft simply because it is styled or classified as a "venture capital" fund. Similarly, provisions of the custody rule that require audits by PCAOB-registered independent accounting firms or the issuance of quarterly reports to investors by a qualified custodian could be adopted by the Commission as a condition of the relevant exemptions. These suggested requirements are consistent with the DFA, which gives the Commission broad authority to define the terms of the relevant exclusions, and with the Commission's broad anti-fraud rulemaking powers under Section 206(4) of the Advisers Act.[15]

II. The Commission Should Require Public Reporting of Census-Type Data Regarding Private Investment Funds, But Should Protect Otherwise Confidential, Proprietary Information.

The Commission is also proposing a substantial expansion of the types of information that it would collect and make publicly available as to investment advisers and private investment funds that they manage. Specifically, investment advisers, including venture capital and private fund advisers that are exempt from registration, would have to report information as to any private funds that they manage on Form ADV. In general, all of this information would be made publicly available via the Commission website and the Investment Adviser Registration Depository ("IARD"). Thus, Section 7B of Schedule D of the Form would be substantially expanded and revised to require reporting and public disclosure of the following information:[16]

- The name of the private fund;[17]
- The state or country of the private fund's organization;
- The names of the general partner, directors, trustees or persons occupying similar positions;

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[14] 17 C.F.R. Section 275.206(4)-2.

[15] We note that these suggestions are also consistent with the conclusions expressed in the *Report on Best Practices for the Hedge Fund Industry* by the Asset Managers Committee to the President's Working Group on Financial Markets, *at* 31, 38, 48 (Jan. 15, 2009).

[16] 75 FR 77065, 77067. To avoid duplication and confusion, an adviser would not have to report funds managed by affiliates, and sub-advisers could exclude private funds that another adviser reports. Similarly, master-feeder funds would be treated as one fund. Advisers with a principal office and place of business outside of the U.S. could omit a Schedule D for any private fund that is not organized in the U.S. and not owned by or offered to U.S. persons. 75 FR 77065.

[17] The Commission proposes that in order to preserve confidentiality, the adviser could supply the code name or number for the fund that it uses in its own files as permitted by Rule 204-2(d)).

- Information as to the organization of the private fund, including as to any master-feeder structures;
- The regulatory status of the fund, including the exception(s) from the Investment Company Act on which it relies;
- Whether the fund relies on an exemption from registration of its securities under the Securities Act of 1933;
- Whether the fund is subject to a non-U.S. regulatory authority;[18]
- Whether the investment adviser is a subadviser to the private fund, as well as the identity (by name and file number) of any other advisers to the fund;
- The gross and net assets of the private fund;
- The type of investment strategy employed by the adviser (to be selected from seven broad categories, such as "hedge," "real estate," "liquidity," and "other");
- A breakdown of the assets and liabilities held by the fund by class and categorization in the fair value hierarchy established under U.S. generally accepted accounting principles ("GAAP");
- The number of investors, their types (whether individuals, government entities, pension funds, other private funds, etc.) and the approximate percentages of ownership by each type, as well as the percentage owned by non-U.S. persons;
- The percentage of ownership of the fund by the adviser and its related persons;
- Minimum investment amounts;
- Whether clients of the investment adviser are solicited to invest in the fund, and the percentage of the adviser's clients that have invested in the fund; and
- The identities of the fund's prime brokers, custodians, auditors, administrators and marketers, related information about such entities, and whether any such entities are related persons of the adviser.

As to the adviser itself, and as to its employees and clients, the Form ADV would be amended to solicit the approximate amount of assets under management by client type, and the approximate percentage of clients that are not U.S. persons. The Form would also

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[18] We note an apparent ambiguity in the Release and proposed Form in this regard. The Release states that Section 7.B will require disclosure of whether the *adviser* is subject to a foreign regulatory authority. 75 FR at 77066. However, the proposed revised Form asks that question regarding the *fund*. 75 FR at 77162. The adviser's status is already required to be disclosed in Schedule D Section 1L.

be revised to require an adviser to reveal whether it does business as, among other things, a registered securities based swap dealer, major security based swap participant or registered municipal adviser. The Form would be amended to require the adviser to state whether it is affiliated with any portfolio brokers, to state whether any "soft dollars" are received consistent with the safe harbor provided by Section 28(c) of the Exchange Act, and to state whether the adviser or any related persons receive compensation for referrals. Advisers would have to provide contact information for a Chief Compliance Officer ("CCO"), if they have one (this information would not be publicly available).[19] Finally, the Form would be revised to require an adviser to disclose if it has $1 billion in assets on the last day of its most recent fiscal year.[20] The Form would not (and should not) reveal any individual's personal financial information.

CPIC has previously advocated for greater transparency of certain information (such as valuation policies, assets under management and certain "census" data) to regulators, investors, potential investors, counterparties and the public. Thus, CPIC supports the Commission's proposed revisions to Form ADV. The additional information that the revised Form will collect should be of assistance to the Commission in its efforts to identify fund advisers, to verify the existence and location of assets and portfolio positions and to carry out general market surveillance. It should also be of use to investors as they conduct due diligence and research the background of fund managers.

Yet, a distinction must be made between information that should be publicly available, and information that should only be reported to regulators for the purposes of law enforcement and the assessment of systemic risk. Thus, as noted above, the Commission is authorized by new Subsection 204(b) of the Advisers Act to require registered investment advisers to maintain records of, and file reports regarding, any private funds that they advise for the assessment of systemic risk by the FSOC, or as necessary and appropriate in the public interest and for the protection of investors. At the same time, Subsection 204(b) contains provisions that direct how information that the Commission receives pursuant to such records and reports must be handled.

Briefly, under Advisers Act Subsections 204(b)(8) and (9), "[n]otwithstanding any other provision of law," the Commission, other government agencies and self-regulatory organizations may not be compelled to disclose reports or records that are required to be maintained or filed under Subsection 204(b). In addition, proprietary information gleaned

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[19] 75 FR at 77069. Exempt Reporting Advisers are not required to have a CCO, but will supply the CCO's contact information if they have one. Otherwise they will supply contact information for another appropriate contact person. Exempt Reporting Advisers will also be required to provide certain limited information regarding their identities, form of organization, disciplinary history, etc.

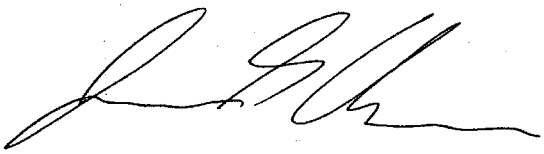
[20] 75 FR 77069. This is proposed in order to implement Section 956 of DFA, which requires the Commission to jointly issue rules with other regulators to require certain financial institutions to disclose to regulators information as to incentive payment structures that are excessive or that could lead to material financial loss, and to prohibit any such arrangements that encourage inappropriate risk.

from such records and reports, such as trading strategies, research methodologies, software and trading data, must be protected from disclosure under the Freedom of Information Act ("FOIA"). Indeed, even the transfer of such reports and records to other regulators must be controlled. Such information may be provided to the FSOC only as necessary for the assessment of systemic risks that are presented by a private fund, and records provided to the FSOC in this regard also must be exempt from public disclosure under FOIA.[21]

The above-described provisions of Section 204(b) reflect a Congressional intent to prevent the distribution of proprietary business data, and we urge the Commission to adhere to this policy.[22] As noted at the beginning of this letter, CPIC has previously supported reporting to regulators of information to assist them in identifying systemic risk. However, public disclosure of certain information, such as position and trading data, could cause substantial harm to investment funds, their investors, their managers and markets in general.

We appreciate this opportunity to provide our comments, and look forward to working with the Commission as it continues with its important work.

Sincerely,



James S. Chanos
Chairman
Coalition of Private Investment Companies

cc: The Honorable Luis A. Aguilar, Commissioner
The Honorable Kathleen L. Casey, Commissioner
The Honorable Troy A. Paredes, Commissioner
The Honorable Elisse B. Walter, Commissioner
Elizabeth M. Murphy, Secretary
Eileen Rominger, Director
Division of Investment Management

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[21] Advisers Act §204(b)(7).

[22] We note the Commission's recent release provides for the confidentiality of such reports. In addition, long-standing Commission rules and practice, as well as federal law and the rules of numerous other federal agencies, recognize the need to protect businesses from the economic and competitive disadvantages that result from public disclosure of such information. For example, Exemption 4 of FOIA (5 U.S.C. § 552(b)(4)) and Rule 80(b)(4) of the Commission's Rules of Practice under FOIA (17 C.F.R. § 200.80(b)(4)) provide that the Commission generally will not publish or make available to any person matters that would "[d]isclose trade secrets and commercial or financial information obtained from a person and privileged and confidential [information]."