April 8, 2021

Via e-mail: rule-comments@sec.gov

Vanessa Countryman, Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

Re: File Number S7-02-21, *Regulatory Flexibility Act Review of "Rules Implementing Amendments to the Investment Advisers Act of 1940"*

Dear Ms. Countryman:

We appreciate the opportunity to comment on the list of rules, adopted in 2011, that are scheduled to be reviewed by the Securities and Exchange Commission (the "SEC") pursuant to Section 610 of the Regulatory Flexibility Act. Our comments pertain only to the "Rules Implementing Amendments to the Investment Advisers Act of 1940."

The Regulatory Flexibility Act sets forth specific considerations to be addressed in the review of each rule. We limit our comments, provided below, to 3 of the 5 considerations listed in 5 U.S.C. 610(b) and referenced in File No. S7-02-21. In summary, we strongly support the continuation of the current rules.

Please feel free to contact Steven Utke (sutke@uconn.edu) if you have questions about this letter.

Sincerely,

/s/ Steven Utke

Steven Utke
Assistant Professor
University of Connecticut

/s/ Paul Mason

Paul Mason
Assistant Professor
Baylor University

I. Background

Release IA-3221 (Federal Register, Vol. 76, No. 138, July 19, 2011) implements rules ("Rules") to give effect to the provisions of Title IV of the Dodd-Frank Act regarding the SEC registration and filing requirements of advisers to private equity, venture capital, and hedge funds (collectively, "private funds" or "funds") previously exempt under the Investment Advisers Act of 1940. The Rules also amend the SEC's Form ADV to facilitate the registration and filing requirements. For example, the revised Form ADV provides *fund-level* rather than only adviser-level information.

The Rules provide both the SEC and the investing public with information not otherwise available. This information is important given that private funds are opaque by their nature, especially compared to public firms. As we discuss below, private funds are supplanting public firms as the primary entities for raising capital in the economy, highlighting the importance of maintaining (or increasing) disclosure by these funds and their advisers.

II. Comments Regarding "Continued Need for the Rule" and "Degree to which… Economic Conditions … Have Changed in the Area Affected by the Rule"

Since the implementation of the Rules, two notable changes have occurred. Both of these changes increase the importance of the Rules. First, the SEC recently expanded the definition of accredited investors in separate rulemaking.[1] Expansion of the accredited investor definition invites a larger number of investors to participate in funds offered by the advisers covered by the Rules, relative to the number of investors able to participate in funds at the time of the Rules' implementation. As such, we view any reduction in the Rules' requirements for adviser registration and information disclosure as unwarranted; increasing market participation in funds increases the importance of the information provided by the Rules.

Second, and relatedly, since the Rules were implemented, private markets – those in which funds covered by the Rules participate – experienced substantial growth while, conversely, public markets shrunk.[2] Given this growth, it is vital to retain the provision of information regarding funds and their advisers under the Rules. In comparison to public firms, whose fundraising is now *less than* that of funds[3], the Rules impose only limited disclosure requirements.

Despite the limited disclosure by private fund advisers, academics are able to gain insight into the operations of private funds from information required to be disclosed under the Rules. While this research area is still developing, the Rules provide adviser and private fund information that allows academic researchers to gain a basic understanding of private funds, which can provide insight for regulators. Importantly, we believe that neither researchers nor regulators fully

[1] Release Nos. 33-10824; 34-89669; File No. S7-25-19.
[2] See, for example: Ewens, M., and J. Farre-Mensa. 2020. The deregulation of private equity markets and the decline in IPOs. *Review of Financial Studies*, forthcoming; Doidge, C., G. A. Karolyi, and R. M. Stulz. 2017. The U.S. listing gap. *Journal of Financial Economics* 123: 464-487.
[3] Witte, P., and G. Brown. 2019. A new equilibrium: Private equity's growing role in capital formation and the critical implications for investors. Ernst & Young and the Institute for Private Capital.

appreciate the important insights – relevant to the SEC's mission – that can be gained from information provided under the Rules.

For example, recent research finds that most private funds, even when exempt from audit requirements, obtain independent audits. Findings suggest that investors' demand for high-quality financial information contributes to exempt funds obtaining audits, suggesting that markets demand more and better information from private funds. However, the audit percentage has decreased over time.[4] Given the likely influx of new investors under the expanded accredited investor rules, and the shrinking of public markets, the SEC may wish to consider investors' demand for private fund information, as well as how the decline in independent audits of private funds, is likely to affect the investing public as well as the SEC's oversight of funds.

Absent the Rules, this insight would be non-existent. We fully expect further insights to develop regarding important attributes of private funds, based on the information required to be disclosed under the Rules.[5] Weakening the Rules will prevent development of these insights and weaken the SEC's ability to regulate funds. Thus, we believe that the SEC's regulatory purpose is well served by continuing the Rules, and by considering an expansion of private fund disclosure. As previously noted, the importance of these disclosures – to both the public and SEC – increases with the increasing importance of private markets.

III. Comment on "Extent to which the Rule Overlaps… with Other Federal Rules"

While we are unable to comment on costs of the Rules directly, we highlight two important aspects of the potential costs. First, while compliance with the Rules certainly requires ongoing, annual costs[6], our view is that there was a substantial start-up cost to comply with the Rules. Once an adviser establishes a process for complying with the Rules, the ongoing costs should be lower than the initial-year costs.

Second, the Rules cover advisers that may also have SEC Form 13F filing requirements.[7] While the Rules cover Form ADV filing requirements, which are separate and independent from Form 13F, we view the fact that advisers already comply with separate SEC requirements as indicative of their ability to comply with the Rules. To the extent possible, we view it as advantageous if the SEC can better connect filings under the Rules (i.e., Form ADV) to other filings (e.g., Form 13F).

Overall, we do not see a strong argument for adjusting the Rules based on cost or compliance considerations. We view the overlap between the Rules and other Federal rules as not only minimal, but actually complementary.

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[4] Gaver, J., P. Mason, and S. Utke. 2020. Financial reporting choices of private funds and their implications for capital formation. Working paper.

[5] Numerous important papers providing these insights are in progress, but not yet publicly available. We encourage the SEC to visit our research websites (https://ssrn.com/author=1688312 or https://ssrn.com/author=2439002) where our work on these topics will be posted when available.

[6] For an estimate of costs, see: Kaal, W. A. 2016. What drives Dodd-Frank Act compliance costs for private funds? *Journal of Alternative Investments* Summer: 8-26. He suggests average costs of $189,150 (470 hours) with a range from $5,000 to $500,000 (50 to 1,500 hours) per adviser.

[7] While Form 13F primarily pertains to hedge funds, other fund types can have Form 13F filing requirements.