



**VIA Electronic Submission**

August 11, 2015

The Honorable Brent Fields  
Secretary  
U.S. Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549-1090

**Re: Proposed Amendments to Form ADV and Investment Advisers Act Rules; File No. S7-09-15.**

Dear Secretary Fields:

On June 12, 2015, the Securities and Exchange Commission (the “Commission” or “SEC”), released proposed rules<sup>1</sup> for public comment that expand the information collected on Form ADV from investment advisers, provide for the umbrella registration of certain affiliated investment advisers on Form ADV, and amend the books and records rule (“Proposed Rules”). The Small Business Investor Alliance (“SBIA”) appreciates the opportunity to comment on these rules and provide our feedback on how they impact advisers to private funds.

SBIA is a national association that develops, supports, and advocates on behalf of policies that benefit investments funds that finance small and mid-size businesses in the lower middle market and middle market, as well as the investors that provide capital to these funds. Our membership consists of traditional 3(c)(1) and 3(c)(7) private funds, funds registered as business development companies (“BDCs”) under the Investment Company Act of 1940, funds that have been licensed or are seeking to be licensed by the Small Business Administration (“SBA”) as small business investment companies (“SBICs”), and the investors that invest in these funds, including high net worth individuals, banks, family offices and pension funds.<sup>2</sup>

The Proposed Rules include positive changes, as well as changes that are of concern to advisers to private funds, and impose burdensome additional reporting and compliance requirements on these funds. As the primary representative of smaller private equity

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<sup>1</sup> Amendments to Form ADV and Investment Advisers Act Rules, 80 Fed. Reg. 33718-33838 (June 12, 2015). All citations and page numbers in this document refer to the version posted on the SEC website at: <https://www.sec.gov/rules/proposed/2015/ia-4091.pdf>.

<sup>2</sup> SBIA currently represents over 200 individual fund advisers, including 32 BDCs (currently there are over 80 BDCs operating in the marketplace).

funds and their advisers, SBIA encourages the SEC to consider strongly the impact on smaller private funds engaging in small business investing while proposing its regulations.

Of particular impact to our members are the changes in the Proposed Rules that permit umbrella registration, and impact the reporting requirements for certain investment advisers on Form ADV.

**I. Umbrella Registration on Form ADV is a Common-Sense and Overdue Modernization and Should be Extended to Exempt Reporting Advisers**

SBIA applauds the SEC for updating Form ADV to permit multiple private fund adviser entities operating a single advisory business to register on a single form. Implementing the guidance put forth in the SEC's 2012 no action letter<sup>3</sup> on umbrella registration was overdue, and recognizes the increasing likelihood that entities may have multiple advisers and funds under their control. The update permitting umbrella registration on Form ADV will make registration and ongoing reporting to the SEC by registered advisers more straightforward for potential investors to digest and conduct due diligence. Umbrella registration provides more clear and consistent information because it creates a centralized location for easy access to the complete picture of a registered investment adviser's structure and business operations. SBIA views umbrella registration of investment advisers as a promising development, and encourages the SEC to implement similar no-action relief into a formal rulemaking in other areas of its jurisdiction, for both advisers and registered funds (including BDCs).

While we appreciate the umbrella registration modernization, SBIA encourages the Commission to also include umbrella registration for multiple exempt reporting advisers ("ERAs") on Part 1A of Form ADV. Many SBIA members are smaller funds and have not yet reached the \$150 million regulatory assets under management ("RAUM") registration requirement. As such, they are classified as ERAs under the changes made to investment adviser registration as a result of the Dodd-Frank financial reform. As the Commission is aware, ERAs must file Part 1A of Form ADV to report to the SEC. However, the proposed rules expressly disallow ERAs from utilizing the umbrella registration process.<sup>4</sup> The SEC's rationale for barring ERAs is based on a perceived effect of ERA umbrella registration compromising data quality and complicating analyses of data from Form ADV. In addition, the SEC states that ERAs are not eligible to utilize umbrella registration because they do not share compliance policies or codes of ethics with registered advisers. The SEC does not provide clear justification as to why ERAs should not receive the benefit of a centralized registration process, and is unclear as to why uniform compliance and code of ethics policies are a necessary component for umbrella registration as it is not fully explained in the Proposed Rules.

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<sup>3</sup> American Bar Association, Business Law Section, SEC Staff Letter (Jan. 18, 2012), available at <http://www.sec.gov/divisions/investment/noaction/2012/aba011812.htm>.

<sup>4</sup> Proposed Rules at f.n. 56.



Similar to consolidated registrations of registered advisers, ERA umbrella registrations would simplify the analysis of data by providing the complete picture of the ERA's structure in one, accessible place. Analyses would be improved because the information would no longer be fragmented. Data quality would not be compromised because the same information is presented. Moreover, Congress explicitly created the ERA exemption in Dodd-Frank to limit the regulatory burdens on smaller private funds. Umbrella registration for ERAs is in line with that mandate, in that it lowers the reporting burden on smaller funds with multiple advisers. In sum, the SEC should permit ERAs to utilize umbrella registration, or further substantiate why it would not make sense to do so in the final rule.

## **II. The Additional Reporting Requirements on Form ADV in the Proposed Rules Fail to Take Into Account ERAs and Unnecessarily Duplicate the Reporting Requirements of BDCs**

SBIA is concerned about the impact on ERAs and external advisers to BDCs as a result of the new information collection requirements on Form ADV. These sections: (1) require investment advisers to report the percentage of a private fund owned by "qualified clients" as defined under Rule 205-3 of the Investment Advisers Act of 1940; and, (2) require investment advisers to report the RAUM of all parallel managed accounts related to a registered investment company or a business development company that is advised by the investment adviser. These new reporting requirements pose challenges and should be reevaluated based on the concerns below.

### Reporting on "Qualified Client" Information Should Follow the Requirements of Rule 205-3, and Only Require that Information at the Time of Subscription.

Requiring investment advisers to calculate the number of "qualified clients" annually is administratively burdensome for advisers to private funds, and in particular may pose significant challenges for ERAs. There are currently three ways in which one can meet the requirements to be considered as a "qualified client" under the SEC regulations.<sup>5</sup> First, you can have \$1,000,000 under the management of the investment adviser.<sup>6</sup> Second, you are an individual with a net worth of more than \$2,000,000, excluding your primary residence and indebtedness secured by that residence from the valuation.<sup>7</sup> Third, you have a connection to the investment adviser as an employee or as an executive of the adviser, among other connections.<sup>8</sup> When adopting Rule 205-3 as a final rule, the SEC stated that "net worth will be calculated only once, at the time the advisory contract is entered into..." for purposes of meeting the "qualified client" test.<sup>9</sup>

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<sup>5</sup> 17 CFR 275.205-3(d)(1).

<sup>6</sup> *Id.*

<sup>7</sup> *Id.*

<sup>8</sup> *Id.*

<sup>9</sup> SEC Release No. IA-3372; File No. S7-17-11 at 14-15 (May 22, 2012), accessible at: <https://www.sec.gov/rules/final/2012/ia-3372.pdf>.

As the drafters of the amendments to Rule 205-3 must have acknowledged, a “one-time only” calculation of net worth saves advisers and investors from having to conduct and respond to extensive information collection on an annual basis. It also is beneficial to investors as it prevents their finances from being evaluated annually. SBIA believes it should be clarified in Form ADV that the information provided on “qualified clients” in the Form ADV must only be provided as of the date the advisory contract was entered into by those “qualified clients.” This will ensure that private fund advisers will not have to add to their burden of collecting this information on an annual basis, nor will investors have to disclose their financials on an ongoing basis to establish that they are qualified.

#### ERAs Should Be Exempted From Reporting on Qualified Clients

In addition to the prior issue, the final rule should specifically exempt ERAs from reporting on qualified clients in Form ADV. As the SEC is aware, section 205 of the Advisers Act pertains only to registered<sup>10</sup> investment advisers. As such, ERAs are not required to collect information on their “qualified clients”, and therefore do not maintain this information. Many ERAs do not have a “qualified client” form in their subscription documents for investors as a result. Requiring ERAs to begin this costly exercise to fill out Form ADV is prohibitive and contrary to the relief provided in section 205 previously for those advisers that are not “registered” with the Commission. As such it would be extremely burdensome to investors and ERAs to begin collecting the relevant financial information and to determine which clients are qualified. As ERAs are ill-equipped to compile the financial information that registered advisers do, the final rule or instructions on Form ADV should exempt ERAs from completing this reporting requirement.

#### Requiring Externally-Managed BDCs to Report the RAUM of “Parallel Funds” Is Duplicative and Unnecessary

The Proposed Rules will now require that BDCs with an external manager report the RAUM of their “parallel managed accounts related to a registered investment company or business development company that is advised by the adviser.”<sup>11</sup> The Commission states that this information will be used to show the extent of “any shift in assets between parallel managed accounts and...business development companies” as well as conflicts of interest between these accounts.<sup>12</sup>

This provision appears to shift Form ADV from a disclosure document into a reporting form, which is not needed because the SEC already is collecting and requiring reports on this information from registered advisers to BDCs in their registration statements. For example, on Form N-2, Item 9 requires that “additional information” be provided about “other accounts managed by the Portfolio Manager(s)...”<sup>13</sup> Item 21 provides that the

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<sup>10</sup> “Registered or required to be registered with the Commission...” Investment Advisers Act of 1940, Section 205(a). Rule 205-3 provides an exemption from the restriction on performance fees in section 205(a) of the Advisers Act.

<sup>11</sup> Proposed Rules at 23-24.

<sup>12</sup> *Id.*

<sup>13</sup> SEC Form N-2, Item 9(1)(c).

BDC must state “the number of other accounts managed within each of the following categories and the total assets in the accounts managed within each category...” including other registered investment companies and other pooled investment vehicles.<sup>14</sup> Further, Item 21 requires:

[a] description of any material conflicts of interest that may arise in connection with the Portfolio Manager’s management of the Registrant’s investments, on the one hand, and the investments of the other accounts included in response to Item 21.1b, on the other. This description would include, for example, material conflicts between the investment strategy of the Registrant and the investment strategy of other accounts managed by the Portfolio Manager and material conflicts in allocation of investment opportunities between the Registrant and other accounts managed by the Portfolio Manager.<sup>15</sup>

Form N-2 also requires the BDC to disclose significant information about any external advisers to the BDC.<sup>16</sup> In addition to the N-2 requirements, BDCs that seek to co-invest in negotiated investments with a parallel managed fund, must receive an exemptive order from the Commission to do so. If this exemptive order is granted, it specifies how conflicts are to be managed between the two entities, eliminating the justification made in the Proposed Rules that this information is needed on Form ADV to evaluate conflicts of interest.

In sum, the SEC is already collecting this information through Form N-2. The Commission also already has mechanisms for dealing with conflicts of interest between these funds. Adding this information to the required information on Form ADV changes the reasoning for that form to more of a reporting document than a disclosure document, and adds duplicative and unnecessary reporting for externally advised BDCs.

The SEC should eliminate this requirement from the final Form ADV. If this requirement is included, it should include a clear definition of the term “parallel managed accounts” to ensure effective disclosure.

### **III. The Proposed Rules Illustrate an Open-Ended Appetite for Additional Reporting and Compliance Obligations, With Harmful Effects on Smaller Fund Advisers**

In the Proposed Rules, the Commission is seeking significantly more information to be included on Form ADV, resulting in more administrative and disclosure burdens for advisers to private funds. This information collection is magnified by the changes to Rule 204-2, and the requirement to collect and maintain copies of performance records. SBIA

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<sup>14</sup> SEC Form N-2, Item 21(1)(b) and (c).

<sup>15</sup> SEC Form N-2, Item 21 (d).

<sup>16</sup> SEC Form N-2, Item 9(b).



is concerned about the SEC's increased focus on requiring more reporting and maintenance requirements on private fund advisers.

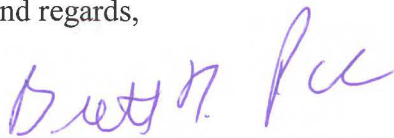
In regard to the changes in the Proposed Rules on Form ADV, SBIA is concerned that the Commission will continue to push the boundaries of Form ADV in the future, requiring more disclosures and reporting beyond that needed to appropriately examine the investment adviser. Such an approach, in the private fund adviser context, will result in a form similar to Form PF, which appropriately is only required to be completed by much larger private fund advisers to address systemic risk concerns. Smaller private funds are less equipped to deal with the overall compliance burden, and pose no systemic risk burden, which is why they are appropriately exempted from completing Form PF.

Likewise, in the changes to the books and records rule, Rule 204-2, SBIA is concerned that this will lead to more document retention requirements for advisers, with those documents being required to be produced at exams. SBIA members already collect and retain most performance information requested in the Proposed Rules for their funds. However, these changes to the books and records rules represent the Commission's interest in requiring advisers to produce significantly more information to the Commission about their advisory activities, including e-mails and other communications between them and their clients. Production of these documents is not overly burdensome, but in aggregate results in increased compliance burdens for smaller private fund advisers.

We encourage the SEC to evaluate the increased overall compliance burden on funds and consider the impact on smaller private fund advisers. Smaller funds, including many of SBIA's members, are often 2-3 person investment advisers, many of which are ERAs that do not have significant back-office staff to assist them with complying with the SEC rules. These funds are small business investors, and are located in many underserved areas of the country where small businesses are starved for capital. If SEC compliance requirements, including the completion of Form ADV and the associated investment adviser rules become too burdensome and expensive to comply with, these funds will be unable to function. If the burden of these rules is not taken into account and funds cannot afford the compliance costs, then small business investment will suffer.

SBIA appreciates this opportunity to share our thoughts on the Commission's Proposed Rules. Please contact Christopher Hayes, SBIA's Legislative and Regulatory Counsel, at [REDACTED] or [REDACTED] if you have any questions regarding this letter.

Kind regards,



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