MANAGED FUNDS ASSOCIATION

Summary of Selected Substantive and Technical Issues
Raised in SEC Comment Letters
Re: Registration of Certain Hedge Fund Advisers

The SEC proposed new rules and amendments to require that certain hedge fund advisers register with the Commission as "investment advisers" under the Investment Advisers Act of 1940. In addition to the letter submitted by MFA, numerous extensive letters were submitted to the Commission in response to the proposal. Many of these letters raised substantive issues and technical concerns about the SEC Proposal. The pages that follow, outlined in the table below, provide a paraphrased summary of points made by certain commentators, categorized by topic, with a reference to the firm or individual that presented the points. This document is intended only to be a summary of key issues and points that MFA has identified in the letters referenced herein; for further details, the letters themselves should be reviewed.

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Submitted October 22, 2004

I. Legal Authority

- Congress has determined that hedge fund investors do not need the protection of registration of hedge fund advisers or hedge funds. **The proposal exceeds the powers granted to the Commission and should be withdrawn.** (Wilmer Cutler Pickering Hale and Dorr LLP)

- **The Congress**, in adopting the Advisers Act and through several amendments, **has recognized that a fund, whether or not exempt from registration under the Investment Company Act of 1940, is itself the client** of an investment adviser and that the several investors in such a fund, if their assets are managed collectively, are not themselves separate advised clients. (Willkie Farr & Gallagher LLP)

- The **legislative history** of the Advisers Act and Investment Company Act indicates that a **hedge fund should be viewed as a single client** for purposes of Section 203(b)(3) of the Advisers Act. (Schulte Roth & Zabel LLP)

- We are particularly concerned that the **Commission is proposing to overturn the policy judgment and factual reality** that underlay Rule 203(b)(3)-1 in its current form, which is the basis on which advisers and investors have operated for decades. (ABA)

- In order to implement the mandatory registration proposal unilaterally the Commission is required to reverse its prior interpretation, adopted nearly 20 years ago, of the meaning of the term "client"…**This new interpretation would be inconsistent with well settled interpretations of the federal securities laws dating back to the 1960s**. (Chamber of Commerce of the United States)

- **If the proposed mandatory registration rule is adopted, the term "client" apparently will have different meanings, one for purposes of determining whether advisers must register and another for other purposes**. We believe such inconsistencies should be avoided unless clearly required as a matter of statutory interpretation. (Chamber of Commerce of the United States)

- We believe that Rule 203(b)(3)-1 as currently written is consistent with Congressional intent, accurately reflects legislative history and represents sound policy—that an adviser's client is the fund, not the investors in the fund. Moreover, we are concerned that **the proposals overstep Commission authority**. (Schulte Roth & Zabel LLP)

- **We question the wisdom of the Commission's approach** in the proposing release **in making "elastic" the term "client" to fit its objective**, absent Congressional action. (Schulte Roth & Zabel LLP)

- The Commission's proposal **is inconsistent with congressional intent and indeed does violence to the statutory pattern**. (Willkie Farr & Gallagher LLP)

- **The Commission does not have the authority to eliminate the statutory exception for investment advisers with fewer than 15 clients** from the registration requirements of the Advisers Act. "The rulemaking power granted to an administrative agency charged with the administration of a federal statue is not the power to make law. Rather, it is the power to adopt regulations to carry into effect the will of Congress as expressed by statute." (Wilmer Cutler Pickering Hale and Dorr LLP)

II. Costs of Registration

- **The Commission materially underestimates the costs of registration** and incorrectly infers that registration imposes only minimal additional burdens. (Davis Polk & Wardwell)

- We have observed the costs incurred by our investment adviser clients in connection with registration and ongoing compliance under the Advisers Act, including the **opportunity costs of time spent away from core asset management duties and the costs of legal and other professional services**. **Our view is that such costs are substantial and increasing and will in some form be passed on to, and affect returns realized by, hedge fund investors**. In addition, we are concerned that offshore advisers, in order to avoid compliance costs and potentially duplicative regulation, may limit the ability of U.S. investors to participate in offshore private funds. (Davis Polk & Wardwell)

- The proposed rule would extend registration and related compliance formalities to hedge funds with as little as $25,000,000 in assets under management. It is reasonable to assume that the management team (if more than a single person) for that quantity of assets would be small. **The imposition of compliance training and compliance formalities on such a small enterprise cannot be anything other than burdensome and a barrier to entry into the hedge fund business.** (ISDA)

- There is also the risk that the proposed rule will force existing mid-size hedge fund -- which do not earn fees sufficient to support the burdensome costs of registration -- to either grow in order to create economies of scale or shrink in order to fall under the $25 million registration threshold. **Because hedge funds tailor their size to a particular investment strategy, this will not only impose additional unnecessary and uncontemplated costs, but is will also depress the efficiency of the hedge fund marketplace.** (ISDA)

- **It is important not to under-estimate the enormous burden of complying with the innumerable technical requirements involved in the *routine* audit process, especially given the complexity of many hedge funds' operations and**

portfolios. All one needs to do is see the voluminous "standard" SEC audit document request list to comprehend the extent of this burden in the hedge fund context. (Sidley Austin Brown & Wood LLP)

- Two hedge fund managers for which we work have each recently spent what we **estimate at between $300,000and $500,000 solely in out-of-pocket costs preparing for and then hosting their SEC auditors—a figure which does not begin to reflect the much greater opportunity costs incurred in terms of the time expended by senior level personnel in connection with the audit**. (Sidley Austin Brown & Wood LLP)

- We are concerned that the use of new products and strategies **raises unnecessary concerns by inexperienced examiners** and other members of the Commission staff and places hedge funds in defensive positions. (Schulte Roth & Zabel LLP)

- **How can a hedge fund manager predict, for example, if the SEC auditors will agree with (or even fully understand) the elaborate and sophisticated valuation procedures which such manager has developed over the years** for esoteric derivatives or with the method in which leveraged performance figures for derived portfolios are explained to highly sophisticated investors? (Sidley Austin Brown & Wood LLP)

- **Many smaller hedge fund advisers cannot afford to hire separate compliance officers** and the role of the compliance officer is assigned to persons serving other critical functions. During a compliance inspection, the person's time and energies are consumed by dealing with the inspection staff, which increases risks to the hedge fund adviser and ultimately to fund investors. (Schulte Roth & Zabel LLP)

- We must take issue with the statements in the proposal that the burdens of registration under the Advisers Act are "minimal" and the costs associated with registration "would not be high." **Registered advisers incur considerable costs** in their commitment to fulfilling their obligations under the Advisers Act. Substantive requirements include: compiling and updating Form ADV, developing and overseeing proxy voting policies and procedures, establishing and implementing a compliance program designed to prevent violations of the securities laws, and developing and enforcing a code of ethics. (ICAA)

- **The new investment adviser compliance program rule alone has resulted in significant, additional costs for many investment advisory firms.** The rule, which was unanimously approved by the Commission, will result in fundamental changes in investment adviser compliance activities and will require a substantial expenditure of time, effort, and resources by all investment advisory firms.(ICAA)

- **The fact is that investment adviser registration and compliance have become increasingly complex and costly.** (ICAA)

III. CFTC Registration

- **SEC should provide an exemption for CFTC-registered CPOs and CTAs that are subject to NFA examination** – to avoid duplicative registration between the SEC and CFTC. (ICAA, City Bar of NY–Cmte on Futures Regulation, NFA, ABA, Katten Muchin Zavis Rosenman, Schulte Roth & Zabel LLP)

- **SEC, CFTC and NFA should work to develop audit programs that address their respective regulatory and compliance concerns** to make use of the expertise of each agency. (City Bar of NY–Cmte on Futures Regulation)

- SEC should provide **clarification of the Section 203(b)(6) exemption as applied to CFTC-registered hedge fund advisers who "primarily" engage in futures** transactions. (Dechert)

IV. Counting Clients

- If a U.S. based adviser advises a non-U.S. fund that has no U.S. investors, is there a compelling reason to require such adviser to count all investors in the fund as clients, rather than simply counting the non-U.S. fund itself as just one client? (Coudert Brothers LLP)

- **The use of the term "securityholders" in Proposed Rule 203(b)(3)-2(a) is broader, and captures a greater universe, than the commonly understood use of the term "investor.**" For example, are persons or institutions that loan money to the fund – such as through preferred securities or investment notes – required to be counted as clients because they may fall within the definition of "securityholder"? (ABA)

- Proposed Rule provides that any relative, spouse or relative of the spouse of a natural person who has the same principal residence counts as a single client. **Should this principle be extended to private funds and to children, spouses of children, and their offspring (and spouses), whether or not they share a residence or are no longer minors?** This would recognize the reality of family tax and estate planning. (ABA)

- In the Proposed Rule, the Commission does not deal with employees of the investment manager as investors in the fund. **Are such employees not counted as clients for purposes of Proposed Rule 203(b)(3)-2(a)** (consistent with the "knowledgeable employee" provision of Rule 3c-5 under the Investment Company Act)? Does a provision allowing only knowledgeable employees to redeem their interests in a fund within two years after their purchase, including because their employment terminates for any reason, cause the fund to be deemed a private fund? (ABA)

- Rule 222-2 under the Advisers Act provides that Rule 203(b)(3)-1 **governs how advisees should be counted for purposes of determining the application of Section 222(d) of the Advisers Act.** Section 222(d) provides that a state may not regulate an adviser if the adviser has no place of business in that state and had fewer than six clients there during the preceding twelve months. If states count investors in a private fund as clients for this purpose, hedge fund advisers may become regulated in numerous states. Should the Proposed Rule have any effect on how advisees are counted for this purpose? (ABA)

- Under proposed Rule 203(b)(3)-2(a), is the counting of clients to be conducted on a fund-by-fund basis or in the aggregate? (Tannenbaum Helpern Syracuse & Hirschtritt LLP)

V. Offshore Advisers/Investors Issues

V.A. General

- In many cases, **offshore advisers use a master-feeder structure whereby offshore investors (and tax-exempt U.S. investors) invest in an offshore feeder, and U.S. taxable investors invest in either a domestic or foreign feeder that is taxed as a partnership**. The Proposed Rule should make clear that the offshore adviser remains exempt from such substantive provisions, even if the domestic feeder (or master fund) is set up as a U.S. entity, so long as the offshore adviser's principal office and place of business are outside the United States. (ABA)

- **The proposed rule maintains the twelve-month look back requirement for counting clients. However, some private funds, particularly non-U.S. funds with non-U.S. advisers, may take steps before the new rule becomes effective to reduce the number of their investors** (or the number of their U.S. resident investors, in the case of non-U.S. funds) to 14 or fewer. Since advisers were not previously required to look through and count investors in private funds as clients, we suggest that the Commission adopt a transition provision permitting advisers to count as clients only investors in private funds at the time the rule becomes effective, without the twelve month look back. (Coudert Brothers LLP)

- SEC should specifically confirm which and **to what extent the substantive provisions of the Advisers Act apply, or do not apply, to registered offshore advisers** as regards their offshore clients with respect to required compliance and ethics programs. (Jonathan Baird)

- SEC should also consider whether the definition of "private fund" includes certain **foreign funds that may have non-U.S. participants who are not "qualified purchasers."** (International Bar Association)

- For offshore funds that are not publicly offered, the "look through" requirement for institutional investors creates a high probability that many EU-based managers will have to register which creates considerable market uncertainty. (FEFSI)

- Rule should clarify whether an offshore fund meets the "private fund" definition if it sells interests to both U.S. and foreign persons, where only the foreign investors have redemption rights. **Do you look only to the conditions of that definition that are met by the U.S. investors,** or do you include non-U.S. (or foreign) investors? (Jones Day)

V.B. U.S. Person Definition

- For non-U.S. funds, **should be able to rely on the definition in Regulation S of "U.S. Person."** (Dechert, FEFSI, International Bar Association, Seward & Kissel)

- Also, Rule excludes from registration requirement private funds that are, among other things, outside the U.S. and are publicly offered outside the U.S. SEC needs to **clarify notions of "public" used in "public investment company" and of "principal office and place of business."** SEC should consider scenarios regarding investment funds which are offered to the public in the EU as UCITs or under individual EU member's state laws, and EU privately placed investment funds which have U.S. resident investors. (European Commission, Investment Management Association)

- Proposed Rule 203(b)(3)-2(d)(3) refers to a fund that, among other things, has "its principal office and place of business outside the United States." **Should whether a fund is "foreign" or not instead turn on the amount and percentage of investor capital it accepts from U.S. persons**, as defined in Rule 902(k) under the Securities Act of 1933? (ABA)

V.C. "U.S. Resident" Definition

- Rule **needs to define "U.S. Resident" for offshore advisers** who need not count clients that are not "U.S. Residents." (International Bar Association, Coudert Brothers LLP, Davis Polk & Wardwell and Guy Lander)

- On the issue of "threshold of assets under management" test for offshore advisers of offshore private funds, "look through" Rule should not apply to **offshore investment advisers of funds, for purposes of the "private adviser" exemption of 203(b)(3), if less than 25% of the value of any class of equity interests in the private fund is held by "U.S. Residents"** (as contained in Regulation S). (International Bar Association)

V.D. Complex Cross-Border Issues

- **Overlapping regulation throws up complex international regulatory issues.** SEC regulation of non-U.S. hedge fund advisers would not guarantee SEC automatic access to those advisers or to enable the SEC to enforce its own regulations against these offshore advisers. (AIMA)

- **Specific conflicting rules** exist **between the FSA rules and SEC rules** in the areas of: (1) trade allocations, (2) conflicting requirements for contracts, (3) limits on performance fees and non-refundable fees, (4) conflicting advertising and marketing rules, (5) compliance manuals that meet both FSA and SEC requirements would be difficult, (6) soft commission and bundled brokerage arrangements are under scrutiny by FSA, (7) conflicting "best execution" rules and (8) proxy voting rules that do not exist in UK. (AIMA)

- Rule **should exclude non-U.S. hedge fund advisers who are subject to adequate local regulation to avoid conflicting and irreconcilable regulations from two or more regulators** covering same ground and a duplication of regulation in relation to authorization, rule compliance, investigations, discipline and enforcement. (AIMA)

V.E. Offshore Publicly-Traded Fund

- Exemption to the definition of "private fund" for certain offshore publicly offered mutual funds. SEC should provide a definition of this term, "offshore publicly offered fund," since the scope and nature of the regulation of such funds varies considerably from jurisdiction to jurisdiction. (Dechert)

- The reference in Proposed Rule 203(b)(3)-2(d)(3) to a fund that **"makes a public offering of its securities outside the United States and is regulated as a public investment company under the laws of the country other than the United States" may be confusing and uncertain when applied**. A number of countries in which offshore funds are organized do not distinguish sharply between public and private offerings and do not impose on investment companies a scheme of regulation such as the Investment Company Act. As a result, it may be difficult to interpret and apply the proposed test. Many offshore funds are offered to investors in more than one country. Would it suffice, for example, under this test if the fund offered some but not all of its shares in a country outside the United States that did differentiate between public and private offerings and regulated public investment pools and private investment pools? Would a fund be deemed to have had a public offering for this purpose if it conducted media advertising or other sales efforts outside the United States that, had they been conducted in the United States, would constitute a "general solicitation" for purposes of Regulation D under the Securities Act? (ABA)

- Section 203(b)(3)-2(d)(3) provides that a non-U.S. fund is not a "private fund" if it "makes a public offering" outside the United States and "is regulated as a public investment company" under laws other than the United States. Can the

Commission clarify that shares of a fund approved for listing on a regulated stock exchange outside the United States meet this qualification? (Coudert Brothers)

V.F. Brochure Requirement for Offshore Advisers

- Should not apply to non-U.S. fund advisers who are regulated in a relevant **jurisdiction** and that the PPM should satisfy this requirement (if that fund is also required to produce a brochure and only advises one or two funds). (AIMA)

VI. Definition of "Private Fund"

VI.A. Two-Year Redemption Criteria

- The rule should clarify that actions taken by an investor to "hedge" its investment in a private fund (such as being a party to a derivative transaction with a third party) will not affect the definition of "private fund." **Such transactions should not affect and should be irrelevant to the two-year lock-up in the definition of a private fund.** (ABA)

- In addition, to exempt venture capital, the two-year lockup on redemptions under the "private fund" definition should be clarified so that this **period begins at the time an investor commits to provide a specific amount of capital to the fund, and that it does not re-start when additional funds are tendered** in response to a capital call. (NVCA)

- Does the two-year lock-up relate solely to the period after an investor contributes capital to a fund and, after such period, the fund may offer more frequent liquidity to such investor? (ABA)

- Proposed Rule 203(b)(3)-2(d)(2)(i) provides that a company is not a private fund if it permits redemption within a two-year period in the case of "extraordinary and unforeseeable" events. The Proposed Rule does not provide any guidance on what types of events would be considered extraordinary and unforeseeable. (Davis Polk & Wardwell, Seward & Kissel, ABA)

- To provide clarity, the Commission should recognize that the general partner or manager of the fund is entitled to determine what constitutes extraordinary circumstances, and that such bona fide determinations will not affect the status of the fund or the adviser. Otherwise, the consequences of the decision will inadvertently affect the adviser and all investors. (ABA)

- Rule should clarify that an investor does not have redemption rights that trigger the look-through rule **if investor has negotiated with fund the right to redeem its interest if certain conditions have not been met**—even if such conditions are not unforeseen or extraordinary events. (Jones Day)

- Clarification needed about **whether redemptions would be permitted if prompted by events beyond the control of the investor that materially alter the investment expectation or the risk/reward ratio** of an investment in the fund. (ABA)

- Clarification needed that **a redemption or exclusion from the fund by the manager and not the investor (such as is typically permitted in hedge funds) would not run afoul of the two-year lock up. (ABA)**

- The Proposed Rule should clarify that debt interests issued by a fund are not relevant to the two-year lock up criteria because they are not "ownership" interests in the sense contemplated by the Proposed Rule. (ABA)

- Rule should clarify **whether certain debt instruments that may be deemed to have redemption rights** would trigger the look-through rule. (Jones Day)

- Under the Proposed Rule, "private funds" include funds that permit their owners to redeem any portion of their ownership interests within two years of the purchase of such interests. In order to avoid market dislocation, **should the Commission make it clear that this provision will only apply to sales of securities from and after such effective date?** (Davis Polk & Wardwell)

- Rule 203(b)(3)-2 should be clarified to state that, "**A right of investors in a fund, by majority or greater vote, to terminate a fund or** to approve or direct the disposition of portfolio assets, **shall not in and of itself constitute a redemption right**." (Gibson Dunn & Crutcher LLP)

- Clarification needed that **the receipt of mandatory distributions would not be deemed a redemption,** and that such a provision would not, in and of itself, cause an investment vehicle to be deemed a "private fund". (Gunderson Dettmer)

- Rule does not make clear that **if a particular investor, but not others, in a fund negotiated a redemption that was less than two years**, **whether this then causes a fund to be a "private fund"** with respect to ALL investors in that fund. Proposed Rule should only apply if substantially all investors have the requisite redemption rights. (Jones Day)

- Rule should clarify whether an investor's right of redemption would trigger the look-through rule **if there is a significant penalty imposed upon that investor's exercising its redemption right.** These penalties are often disincentives for investors to exercise their redemption rights. (Jones Day)

- When a private fund is organized as a limited partnership, the sponsor will create one entity to be the investment manager and another to serve as the "general partner" of the fund. Both entities receive compensation and could be deemed to be providing investment advice, so both could be required to register. There is no

policy that would be served if both the IM and the GP had to register. **The fund's general partner (GP) or managing member should not be required to register** if: (1) GP only serves as general partner, (2) investment manager treats books and records of the GP as its own, and (3) any incentive compensation is treated as subject to Section 205 of Advisers Act. (Dechert)

- Proposed Rule 203(b)(3)-2(d)(2)(ii) provides that a company is not a private fund if it permits redemptions within a two-year period in the case of "reinvested dividends**." In light of the fact that many investment entities are organized as partnerships or limited liability companies that do not issue "dividends," the language should be revised to read "dividends, allocated profits or other returns on invested capital, whether or not distributed."** This should include any distributions or allocations of profit to investors from the capital invested in the fund, as well as distributions made to allow investors to satisfy their tax obligations (many fund agreements allow or require general partners to make annual tax distributions to their investors). (ABA)

- Footnote 140 of the Proposing Release states that the two-year redemption test would apply to each investment in the fund, not only the initial investment. **If the Commission determines that any additional investments are subject to a new two- year lock-up period, should the final rule provide that the additional investment will not extend the lock-up period of the initial or any other investment?** (ABA)

VI.B. <u>Distinguishing Venture Capital, Private Equity</u>

Is there a justifiable basis for distinguishing between the advisers covered by the proposed rulemaking and advisers to venture capital and private equity funds? Are there risks that are peculiar to hedge fund advisers? (Dissent by Commissioners Glassman and Atkins)

- Proposed Rule could also create a safe harbor from registration requirement based on the composition of the fund's investment portfolio with respect to **funds that invest in debt/equity securities that are not publicly-traded**. (Gibson Dunn & Crutcher LLP)

- Clarification needed that an investor's right to participate in an election to dissolve a private equity fund would not, in and of itself, cause an investment vehicle to be deemed a "private fund" under the Proposed Rules. (Gunderson Dettmer)

- Clarification is needed that the **existence of a limited withdrawal right would not, in and of itself, cause an investment vehicle to be deemed a "private fund" under the Proposed Rules**. (Gunderson Dettmer)

VI.C. <u>Subadvisers/Funds of Hedge Funds</u>

- On the issue of subadvisers, in the definition of private fund, the third prong of the definition says that the fund is a company "interests of which are or have been offered based on the investment advisory skills…" **What if the advisor contracts out advisory skills to a sub-adviser?** (Richard Spears Kibbe & Orbe LLP)

- One of the proposed requirements of the definition of "private fund" is that interests in the fund have been "offered based on the investment advisory skills, ability or expertise of the investment adviser". **Can the Commission clarify that if the adviser to a private fund has the ability to engage subadvisers from time to time in the adviser's discretion, and if the identity of a particular subadviser engaged by the adviser to manage assets for the private fund is not disclosed to prospective investors in offering materials for the private fund, then the sub-adviser should not have to look through and count investors in the private fund in determining the number of clients of the sub-adviser**? (Coudert Brothers LLP)

- Under Rule, hedge fund advisers to funds in which a registered investment company (RIC) invests would have to count investors in that RIC. Same rule would apply in **the case of an investment in a private fund by an unregistered fund of funds.** The adviser to the underlying fund would receive from the adviser to top-tier fund that the top-tier fund has more than 14 clients/owners. This makes planning by the underlying manager impossible. A registration obligation could be triggered by circumstances outside underlying manager's control. This is even more problematic in the context of an offshore adviser to an offshore fund. (Dechert)

- Footnote 125 of the Proposing Release states that in a multi-tier structure, the Proposed Rule would "compel looking through the top-tier fund." **Is the look-through required only if, at the time the fund of funds acquires any securities of the underlying fund, such fund of funds owns at least 10% of the capital of the underlying fund?** (ABA)

- In the event the Commission continues to require a "look through" of top-tier investors, **are private fund advisers able to rely on the representations of the top-tier investor at the time of the investment in the fund, and not required to monitor this information on an ongoing basis**? (Seward & Kissel LLP)

- In a multi-tier, or fund of hedge funds situation, **does the adviser owe the investors in the investment entities that invest in the private fund (when the adviser is not rendering investment advice directly to such investors) a brochure and other documentation given to clients**? (ABA)

- If the adviser to a hedge fund that has 15 or more investors engages a sub-adviser, **is the sub-adviser required to register under the Advisers Act if it does not have 14 or more other U.S. clients**? (ABA)

- **The Commission should make clear that, in a situation where a fund of hedge funds invests in a downstream hedge fund, the adviser of the fund of hedge funds should determine the suitability for its investors of the investment in the downstream fund.** The adviser to the downstream fund should not be obliged to determine whether that investment was suitable for the investors in the fund of hedge funds or to assess whether the individual investors in the fund of hedge funds would have met the downstream fund's suitability criteria if they had sought to invest directly. (ABA)

VI.D. Other Issues Related to "Private Funds" Definition

- Clarification needed as to when an investor would, or would not, be deemed to have made an investment "based on the ongoing investment advisory skills, ability or expertise of the investment adviser." (Gunderson Dettmer)

- Under Rule 203(b)(3)-1(a)(2)(i) the term "other security holders" has been added, which would trigger the look through. Rule is unclear if this applies to offshore **funds with holders of "capital notes" or "income notes."** What about holders of **"commercial paper", "medium term notes" and "long term bonds"?** (Jones Day)

- Definition of **"private fund" should exclude "Multi-Generational Family Funds."** (Skadden Arps)

- Clarification needed that the determination of whether a fund falls within definition of a "private fund" must be made on a prospective basis. (Katten Muchin Zavis Rosenman)

VII. Amendments to Form ADV

- **The Commission should clarify the use of the term "client" throughout Form ADV as it relates to investment advisers to hedge funds.** The current Form ADV is unclear and inconsistent, sometimes seeming to regard the hedge fund and sometimes seeming to regard its investors as the adviser's clients. If the Proposed Rule is adopted, an abundantly cautious adviser would likely use its definition of "client" for all responses in the Form ADV. This could impair the accuracy of the data that the Proposed Rule seeks about hedge fund advisers and the hedge funds they manage. (ABA)

- **Will a "private fund" lose the exemption** from registration provided by Section 4(2) of the Securities Act, or Rule 506 thereunder, as a result of reporting that fund on Section 7.B. of Schedule D of Part 1 of the Form ADV? (ABA)

VIII. Custody Rule Issues for Fund of Hedge Funds

- With respect to funds of hedge funds, **the extension of the time period for delivering audited financial statements to 180 (from 120) should *only* apply to a manager of fund of funds**. The underlying funds would still have to meet the 120-day rule, giving the fund of funds manager 60 additional days to prepare audited financials for investors. (Dechert, Renaissance Technologies, Coudert Brothers LLP, Katten Muchin Zavis Rosenman, Tannenbaum Helpern Syracuse & Hirschtritt LLP, Van Hedge Fund Advisors, and Strook)

IX. Books and Records/Performance Records

- Clarification is needed that the exemption provided by the **Transition Rule for the "books and records [that] pertain to the performance or rate of return of [a] private fund" includes those records that pertain to the prior performance of accounts other than the private fund itself that are being used** (consistent with the staff's prior interpretations) in advertisements for the private fund (so-called "model performance"). The requirements imposed by existing staff guidance with respect to such model performance would ensure that it is presented in a non-misleading manner. (Drinker Biddle & Reath)

- What does the Commission consider to be adequate documentation? (James E. Mitchell)

X. Definition of Qualified Clients

- Amendments to **Rule 205-3 regarding "qualified clients" should exempt family members of such clients** from the minimum net worth and minimum investment requirements so that qualified clients may invest on behalf of their children. (Maynard Capital Partners)

XI. Registered Investment Company Issues

- Will there be a **specific statutory form for investment advisers of "private funds" to furnish to investors that are registered investment companies to obtain the number of investors**? Alternatively, is obtaining an oral representation that the registered investment company has more than fourteen owners sufficient to satisfy proposed Rule 203(b)(3)-2(b)? (Tannenbaum Helpern Syracuse & Hirschtritt LLP)

- **What is the time period for obtaining such information from an investor that is a registered investment company**? *E.g*. is the investment adviser obligated to obtain the information three days, ten days or thirty days before an investment by a registered investment company? (Tannenbaum Helpern Syracuse & Hirschtritt LLP)

- Will an investment adviser have to **obtain an annual re-certification** from an investor that is a registered investment company to ensure that the information is not stale? (Tannenbaum Helpern Syracuse & Hirschtritt LLP)