

WILL PRIVATE EQUITY DODGE THE REGISTRATION BULLET?

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To Our Clients and Friends:

The initial U.S. financial system regulatory reform proposals would have required that all advisers to private investment funds (including hedge funds, private equity funds and venture capital funds) register with the Securities and Exchange Commission under the Investment Advisers Act of 1940. However, a discussion draft proposed on Tuesday by Senator Dodd, chairman of the Senate Banking Committee, would exempt advisers to venture capital and private equity funds from the proposed registration requirements, probably on the basis that these types of funds pose no real systemic risk to the financial system. The discussion draft still contemplates that advisers to hedge funds would be required to register under the Advisers Act.

The first movements to scale back the proposal to require the registration of private fund advisers occurred in the U.S. House of Representatives, where draft legislation contained an exemption for advisers to “venture capital funds.” This in turn spurred an attempt to provide similar exemptions for advisers to small and mid-size private funds. Specifically, the bill emerging from the House Financial Services Committee markup provides an exemption from registration for advisers that only advise private funds each of which has less than \$150 million under management. Such small private fund advisers would still be required to maintain certain records and provide certain reports as the SEC determines are necessary or appropriate either for the protection of investors or in the public interest. In addition, the House bill also directs the SEC to tailor the registration and examination requirements for advisers to “mid-size” private funds according to the level of systemic risk that they present.

The discussion draft proposed on Tuesday by Senator Dodd goes even further than the House bill. Under Senator Dodd’s proposal, advisers to “venture capital funds” and “private equity funds” would be exempt from the registration requirements of the Advisers Act. Under the proposal, advisers to “private equity funds” would be subject to certain recordkeeping and reporting obligations as determined by the SEC. The SEC would be responsible for defining which funds are “venture capital funds” and “private equity funds.”

The likelihood that private equity fund sponsors will be required to register under the Advisers Act has decreased as the justification for private fund adviser registration has narrowed to focus principally on systemic risk. The exemptions discussed above will likely be revised, and could be eliminated, as the legislative process advances. The Senate legislation, in particular, is far from final. Even when legislation finally is enacted, the new

regulatory landscape for private equity funds will not be entirely clear until the SEC has finished its rulemaking.

Please call us if you have any questions.

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