SKRC

COMPLIANCE ALERT

MAY 2017

Key Impacts on Private Equity Industry of House Proposals

On May 2, 2017, the United States House Committee on Financial Services began considering the proposed Financial CHOICE Act (the "Proposed Act"), a bill sponsored by Committee Chairman Jeb Hensarling (R-Texas). The Proposed Act includes provisions of particular importance to private equity fund advisers as well as the funds that they manage.[1]

Specifically, Section 858 of the Proposed Act would reverse current law by exempting private equity fund advisers from the investment adviser registration and reporting requirements of the Investment Advisers Act of 1940. The SEC would issue final rules to define the term "private equity fund." The SEC would also issue final rules to require private equity fund advisers to maintain such records and to provide it with such annual or other reports as the SEC determines is necessary and appropriate, taking into account fund size, governance, investment strategy, risk and other factors. The Proposed Act does not discuss how these reports would be filed and whether they would be publicly available, such as a Form D, or not publicly available, such as a Form PF.

Further, Section 860 of the Proposed Act would expand the definition of "accredited investor" under Regulation D of the Securities Act of 1933, the private placement rules relied upon by most private equity funds. The expanded definition would include those natural persons currently licensed as broker-dealers or investment advisers by the SEC, FINRA, another self-regulatory organization or a state securities agency. Moreover, the term "accredited investor" would include any natural person that the SEC determines to have demonstrable education or job experience to qualify as having professional knowledge related to a particular investment, and whose education or job experience is verified by FINRA or another SRO (which, based on past SEC statements, could include accountants and attorneys, among others). Note that there is currently no analogous change proposed in the context of the exemptions from registration under the Investment Company Act of 1940 relied upon by most private equity funds. This effectively means that the proposed expansion of the "accredited investor" definition would have little consequence for "Section 3(c)(7) funds" which, independent of Regulation D, have their own much higher "qualified purchaser" financial requirements.

SKRC Observations

The Proposed Act is still in its very preliminary stages. Seward & Kissel Regulatory Compliance (SKRC) will be monitoring the Proposed Act very closely in order to keep our private equity clients apprised of any new developments that may affect their businesses. Until the proposals are enacted, private equity fund advisers remain subject to the registration and other requirements of the Advisers Act and, even if passed, we expect that most managers would continue to maintain a robust compliance program, especially in light of the demands of institutional investors. Moreover, with respect to the proposed accredited investor changes, we anticipate that the SEC will seek public comment, especially with respect to the professional knowledge category.

SKRC offers comprehensive compliance consulting services to private equity fund managers under tailored fixed fee arrangements. SKRC's services include SEC registration, compliance policies and procedures, ongoing compliance consulting, mock audits and SEC exam representation. For more information on SKRC, please contact David Tang at tang@sewkis.com or (212) 574-1260.

[1] The full text of the Proposed Act is available here. The Proposed Act includes many other notable provisions, including the repeal of the Department of Labor's Fiduciary Rule, the repeal of the Volcker Rule under the Dodd-Frank Wall Street Reform and Consumer Protection Act and amendments that affect the prohibition on general solicitations under Regulation D of the Securities Act of 1933.

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