

THE PRIVATE FUNDS BULLET REPORT

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Business Planning, Structural, Legal, Regulatory & Compliance Developments

- On December 21, 2011, the SEC issued a [final rule](#) implementing the requirement that a natural person's primary residence be excluded for the purposes of determining if a person qualifies as an "accredited investor" under the \$1,000,000 net worth test. The final rule clarifies that debt secured by a person's primary residence will be regarded as a liability if it exceeds the fair market value of the property, and debt less than or equal to the fair market value will only be counted as a liability if incurred within 60 days of the subscription. The final rule provides an exception for pre-committed capital by existing investors in private funds, but otherwise has no grandfathering provisions. Note that the SEC has not issued a final rule implementing the changes with respect to the "qualified client" net worth test set forth in Rule 205-3 of the Advisers Act.
- The recently established SEC Advisory Committee on Small and Emerging Companies has issued a [recommendation](#) that the SEC permit general solicitation and general advertising in private offerings under Rule 506 of Reg D to accredited investors with whom firms do not have a pre-existing relationship.
- In December 2011, the IRS issued [temporary regulations](#) regarding the reporting of "specified foreign financial assets" under Internal Revenue Code Section 6038D. Under these rules, a U.S. individual who is a direct investor in an offshore fund will generally be required to report such investment on IRS Form 8938 beginning with the 2011 calendar year. These rules do not contain any attribution rules that require reporting of indirect interests in offshore funds, and do not require any additional filings by tax-exempt entities. These requirements are in addition to any requirements under the FBAR rules.
- A December 1, 2011 [press release](#) by the SEC announced a new initiative, the "Aberrational Performance Inquiry", pursuant to which the SEC will analyze hedge fund returns and attempt to identify "performance that appears inconsistent with a fund's investment strategy or other benchmarks." If a fund's performance is identified as aberrational, the SEC may engage in further scrutiny of the fund's business.
- In December 2011, the Senate Homeland Security & Governmental Affairs Committee [passed](#) the "STOCK Act" to prohibit Members of Congress from trading securities on nonpublic "political intelligence." The [House version](#) of the bill expands the prohibition to all persons, including asset managers, that are in possession of material nonpublic information obtained from federal sources.
- On January 4, 2012, the Office of Compliance Inspections and Examinations of the SEC issued a [National Examination Risk Alert](#) setting forth the staff's view on registered investment advisers' use of social media. The alert offers a list of non-exhaustive factors that an adviser may want to consider in evaluating its existing compliance policies regarding the use of social media. The staff also reminded firms that allowing third-party postings may violate the prohibition against the publication of testimonials and that recordkeeping requirements apply to social media communications.
- At an anti-money laundering conference held on November 15, 2011, James H. Freis, Jr., Director of FinCen, [announced](#) that the agency is working on a proposal that would require investment advisers to establish AML programs and to report suspicious activity.

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