Clients&FriendsMemo

SEC Issues No-Action Letter Addressing Registration Requirements for Certain Advisory Affiliates

February 13, 2012

The staff of the Securities and Exchange Commission (the "Commission") issued a no-action letter on January 18, 2012 to the American Bar Association's Subcommittee on Hedge Funds clarifying the registration requirements for certain related entities under the Investment Advisers Act of 1940, as amended (the "Advisers Act").[1] The letter reaffirms and clarifies the Commission's previously existing position that registered advisers to private funds may file a single Form ADV that includes special purpose vehicles ("SPVs") established to function as general partners or managing members of a fund. In addition, the letter explains the conditions under which a group of related advisers organized as separate legal entities, but operating as a "single advisory business," may elect to file a single Form ADV.

Clarification of 2005 Registration Guidance for Advisers with Associated SPVs

In a no-action letter issued in 2005 (the "2005 Letter"), the Commission stated its position that an SPV established by a registered adviser to act as a general partner or managing member of a fund would not need to separately register with the Commission, subject to certain enumerated conditions.[2] Instead, the SPV would essentially look to, and rely upon, the filing adviser's registration. In its recent letter, the Commission staff reaffirmed this position and clarified its scope.

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[1] A copy of that no-action letter, issued in response to an inquiry from the American Bar Association's Subcommittee on Private Investment Entities, can be found here: http://www.sec.gov/divisions/investment/noaction/2012/aba011812.htm.

[2] These conditions are:

- The investment adviser to a private fund establishes the SPV to act as the private fund's general partner or managing member;
- The SPV's formation documents designate the investment adviser to manage the private fund's assets;
- All of the investment advisory activities of the SPV are subject to the Adviser's Act and the rules thereunder, and the SPV is subject to examination by the SEC; and
- The registered adviser subjects the SPV, its employees, and persons acting on its behalf to the registered adviser's supervision and control and, therefore, the SPV, all of its employees, and the persons acting on its behalf are "persons associated with" the registered adviser (as defined in section 202(a)(17) of the Adviser's Act.)

While the 2005 Letter specifically addressed the case of a registered adviser that had established a single SPV, the staff confirmed the 2005 Letter's applicability to a registered adviser that has established multiple SPVs. Furthermore, despite the condition that the registered adviser must subject the SPV, its employees, and any persons acting on its behalf to supervision and control, the staff's recent letter expanded the position's applicability to an SPV with independent directors. In order for the guidance to apply, however, every other condition set forth in the 2005 Letter must be satisfied, and these independent directors must be the only persons acting on the SPV's behalf that are not subject to the registered adviser's supervision and control.

Additional Registration Guidance for Multiple Related Entities Conducting a "Single Advisory Business"

For any number of reasons—operational, tax, legal, regulatory or otherwise—an adviser to a private fund may be part of a group of related advisers. These advisory affiliates may be organized as separate legal entities, but may maintain aspects of a collective operation so as to form a "single advisory business."

The January 18, 2012 letter set forth the conditions under which these affiliates may rely upon the registration of the filing adviser to satisfy any obligation they may have to register with the Commission, in lieu of registering separately. To qualify, each relying adviser must be controlled by, or be under common control with, the filing adviser. In the absence of any evidence indicating that the advisers are engaged in different businesses, the Commission would view the filing adviser and one or more relying advisers as operating a "single advisory business" (and thus as eligible to rely upon a single registration) if all of the following conditions are satisfied:

- The filing adviser and each relying adviser advise only (i) private funds and (ii) separate account clients that are "qualified clients" (as defined in Rule 205-3 promulgated under the Advisers Act), and are otherwise eligible to invest in the private funds advised by the filing adviser or a relying adviser, and whose accounts pursue investment objectives substantially similar or otherwise related to those private funds.

- Each relying adviser, its employees, and persons acting on its behalf are subject to the filing adviser's supervision and control and thus are considered "persons associated with" the filing adviser.

- The filing adviser must have its principal place of business in the United States and, therefore, all of the substantive provisions of the Advisers Act and the rules thereunder apply to the filing adviser's and each relying adviser's "dealings with each of its clients, regardless of whether any client or the filing adviser or relying adviser is a United States person."

- The advisory activities of each relying adviser are subject to the Advisers Act and the rules thereunder, and each relying adviser is subject to Commission examination.

- The filing adviser and each relying adviser operate under a single code of ethics and a single set of written policies and procedures, adopted in accordance with the Advisers Act and administered by a single chief compliance officer.

- The filing adviser must disclose in the Miscellaneous Section of Schedule D of its Form ADV filing that it is making a single filing together with its relying advisers. This disclosure should reference the guidance expressed in the Commission's recent letter. The filing adviser should further identify each relying adviser by completing a separate Section 1.B., Schedule D, of Form ADV for each relying adviser and by including the notation "(relying adviser)."

The Commission's position has important implications for U.S.-based filing advisers with advisory affiliates located abroad. A significant question arises as to whether a foreign investment adviser would want to be perceived as operating the same advisory business as its U.S. affiliates and be fully subject to all of the requirements contained in the Advisers Act. Note, in this regard, that if such an adviser registered separately with the Commission, most of the substantive provisions of the Advisers Act would not be applicable to the adviser's relationship with its non-U.S. clients. Further, note that the filing adviser, which must be located in the U.S., would be required to be the firm that is in "control" of the other advisers, which may raise complicated issues of corporate structure and governance, particularly if the non-U.S. adviser is an affiliate but not a subsidiary of the U.S. adviser.

While the Commission's guidance permits a filing adviser and any relying advisers to file a single Form ADV, such a decision is elective, and the entities may continue to file separately if they so choose. Also note that, to rely on the January 18, 2012 letter, the filing adviser and each relying adviser must not be prohibited from registering with the Commission by Section 203A of the Advisers Act.

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Please feel free to contact any of the following Cadwalader attorneys if you have any questions about this memorandum.

Drew G.L. Chapman	+1 212 504 6540	drew.chapman@cwt.com
Steven D. Lofchie	+1 212 504 6700	steve.lofchie@cwt.com
Maurine R. Bartlett	+1 212 504 6218	maurine.bartlett@cwt.com
Zahra F. Zaidi	+1 212 504 6567	zahra.zaidi@cwt.com