

Morgan Lewis

together  
Morgan Lewis Hedge Fund University™  
Form PF: What You Need to Know

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# Today's Presenters



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# Key Topics

- Primary Topic:
  - SEC Form PF
    - *General overview*
    - *Particular issues*
- Additional Topic (time permitting)
  - Treasury International Capital Reporting System

# SEC Form PF

# Form PF - Overview

- In October 2011 the SEC and the CFTC jointly adopted new rules to implement Sections 404 and 406 of the Dodd-Frank Act.
- The rules require investment advisers registered with the SEC that advise one or more private funds to file “Form PF” with the SEC, on a confidential basis.
- The purpose of Form PF is to gather information to assist the Financial Stability Oversight Council (also created by the Dodd-Frank Act) in monitoring and responding to systemic risks to financial market stability.
- Designed to supplement Form ADV disclosure, which was also recently revised to include more detailed private fund information.
- The frequency and detail of the filing requirement depends on the type of private funds advised, as well as the adviser’s total relevant regulatory assets under management (“RAUM”).

# Form PF – Who Must File

- Any investment adviser that is registered (or required to be registered) with the SEC (including jointly registered commodity pool operators or commodity trading advisors) that advises at least \$150 million of private fund assets as of the end of the adviser’s last fiscal year must file at least Section 1 of Form PF.
  - “Private funds” are defined as 3(c)(1) or 3(c)(7) funds under Section 202(a)(29) of the Investment Advisers Act.
  - “Regulatory assets under management” are calculated gross of outstanding indebtedness and other accrued but unpaid liabilities.
- Advisers that are not required to register (e.g., “family offices” under Section 202(a)(11)(G)) or are exempt from SEC registration (e.g., “venture capital fund advisers” under Section 203(l) and “private fund advisers” under Section 203(m)) need not file Form PF.

# Form PF – Who Must File

- The more you manage, the more information you must report and the sooner you have to report initially.
- The additional reporting requirements are broken down by types of funds managed:
  - Hedge funds (\$1.5 billion hedge fund RAUM)
  - Liquidity funds (\$1 billion liquidity fund RAUM)
  - Private equity funds (\$2 billion private equity fund RAUM)
- Due dates for initial filings are further differentiated by RAUM size.
  - Advisers with \$5 billion RAUM within a specific fund category must report **during summer 2012**.

# Form PF - RAUM

- Regulatory Assets Under Management (RAUM)
  - Calculated in accordance with Part 1A, Instruction 5.b of Form ADV.
    - *Gross (not net) basis: without deduction of any outstanding indebtedness or other accrued but unpaid liabilities.*
    - *Cannot deduct accrued fees, expenses or the amount of any borrowing.*
  - Securities portfolios for which the adviser provides continuous and regular supervisory or management services, regardless of whether the assets are family or proprietary assets, assets management without receiving compensation, or assets of foreign clients.
    - *An adviser must include the value of any private fund over which it exercises continuous and regular supervisory or management services, regardless of the nature of the assets held by the fund.*
    - *Sub-advisers to private funds include only that portion of the value of the portfolio for which it provides continuous and regular supervisory or management services.*
    - *Discretionary authority over fund assets (or a portion of fund assets) and the provision of ongoing supervisory or management services satisfies the definition of “continuous and regular.”*
  - Must include the amount of any uncalled capital commitments made to a private fund.
  - Must use the market value of private fund assets, or the fair value of the private fund assets where the market value is unavailable.
    - *Cannot elect to value assets based on cost.*
    - *Shorts are not netted.*



# Form PF - Aggregation

- In determining its reporting classification, an adviser must aggregate with its private fund assets:
  - “Parallel managed accounts” that pursue substantially the same investment objective and strategy and invest in substantially the same positions;
    - *Unless such parallel managed accounts exceed the value of the adviser’s private fund assets (these are referred to as parallel managed account that are not “dependent”)*
  - Private fund assets advised by “related persons” that are not “operated separately” from the adviser; and
  - Master-feeder structures.

# Form PF - Aggregation

- “Separately Operated” factors:
  - No business dealings with the related person in connection with advisory services provided to clients;
  - No shared operations with the related person;
  - No client or business referrals to the related person (and vice-versa);
  - No shared supervised persons or shared premises with related person; and
  - No reason to believe that the relationship otherwise creates a conflict of interest with your clients.
- Parallel managed accounts of related persons not operated separately must also be aggregated, unless they are not “dependent” parallel managed accounts.

# Form PF - Aggregation

- Example (from SEC FAQs):
  - Adviser has \$600 mm AUM in Hedge Fund 1
  - Related Person has \$300 mm AUM in Hedge Fund 2
  - Related Person has \$800 mm in Managed Account 1
  - Adviser and Related Person are not separately operated
  - Hedge Fund 1, Hedge Fund 2 and Managed Account 1 all pursue substantially similar investment objectives and strategies and maintain substantially similar positions (i.e., they are “parallel”)
  - Result: Hedge Fund 1 and Hedge Fund 2 are aggregated together; Managed Account 1 is a dependent parallel managed account because \$800 mm < \$900 mm and, therefore, Managed Account 1 is also aggregated. Adviser has \$1.7 bn in hedge fund AUM and thus is subject to Section 2 reporting.

# Form PF - Aggregation

- Modified Example (from SEC FAQs):
  - Adviser has \$600 mm AUM in Hedge Fund 1
  - Related Person has \$300 mm AUM in Hedge Fund 2
  - Related Person has \$800 mm in Managed Account 1
  - Adviser and Related Person are not separately operated
  - Hedge Fund 1 and Hedge Fund 2 are not parallel
  - Hedge Fund 1 and Managed Account 1 are parallel
- Result: Hedge Fund 1 and Hedge Fund 2 are aggregated because they are not separately operated. Managed Account 1 is not a dependent parallel managed account of Adviser, because \$800 mm > \$600 mm. Managed Account 1 is not aggregated with Hedge Fund 1, and Adviser has \$900 mn hedge fund AUM, and is subject to Section 1 reporting only.

# Form PF - Classifications

- Large Advisers to Hedge Funds
  - At least \$1.5 bn in RAUM in “hedge funds” as of the end of any month during the prior fiscal quarter (i.e., for September 30<sup>th</sup> quarter end, you look back to April, May and June month ends).
  - Report Sections 1 and 2 of Form PF.
  - Hedge funds include:
    - *Private funds that include a performance fee based on market value (instead of being limited to realized gains);*
    - *Private funds that are highly leveraged;*
    - *Private funds that engage in short selling; and*
    - *Private funds that are permitted to use leverage or sell short, even if there is no present intention to do so.*

# Form PF - Classifications

- Large Advisers to Hedge Funds
  - Hedge funds do not include:
    - *Securitized asset funds;*
    - *Private funds that use performance fees solely for financial reporting and which are not paid to the adviser; or*
    - *Private funds that engage in short sales solely for hedging currency exposure or managing duration.*
  - Required to report quarterly within 60 days of quarter end.
  - Commodity pools should be categorized as hedge funds for reporting purposes.
    - *The SEC has indicated a private fund should be treated as a “commodity pool” (and therefore as a “hedge fund”) if the fund’s commodity interest position exceeds either of the de minimis tests under CFTC Rule 4.13(a)(3)(ii).*

# Form PF - Classifications

- Large Advisers to Liquidity Funds
  - At least \$1 bn in RAUM in “liquidity funds” and registered money market funds (in the aggregate) as of the end of any month during the prior fiscal quarter (i.e., for December 31<sup>st</sup> quarter end, you look back to July, August and September month ends).
  - Report Sections 1 and 3 of Form PF.
  - Liquidity funds include:
    - *Private funds that seek to generate income by investing in short-term obligations in order to maintain a stable NAV or minimize principal volatility.*
  - Required to report quarterly within 15 days of quarter end.

# Form PF - Classifications

- Large Advisers to Private Equity Funds
  - At least \$2 bn in RAUM in “private equity funds” as of the last day of prior fiscal year.
  - Report Sections 1 and 4.
  - Private equity funds include:
    - *Private funds that are not hedge funds, liquidity funds, real estate funds, securitized asset funds or venture capital funds (each as defined in Form PF) and that do not provide redemption rights in the ordinary course.*
  - Required to report annually within 120 days of FYE.



# Form PF - Classifications

- The SEC has indicated that private fund categorizations may change from one reporting period to the next, which may affect the adviser's classification under Form PF.
- Fund categories are not mutually exclusive, so certain private funds may be both “liquidity funds” and “hedge funds.”
  - The SEC has indicated that such funds should be included in RAUM calculation of both fund categories and relevant information should be reported in both Form PF sections.
  - For example, an RIA with a single private fund with \$1.6 bn in assets that meets the definitions of both a “hedge fund” and a “liquidity fund” would have to report on Sections 1, 2 and 3.

# Form PF – Initial Filing Dates

- An adviser's initial filing date depends on its classification and its fiscal year/quarter.
- \$5 bn RAUM within any classification triggers earlier initial filing dates
- Assuming a calendar fiscal year, the following apply:
  - July 15, 2012 – more than \$5 bn in liquidity fund RAUM
  - August 29, 2012 – more than \$5 bn in hedge fund RAUM *(5 weeks away)*
  - January 15, 2013 – between \$1.5 and \$5 bn liquidity fund RAUM
  - March 1, 2013 – between \$1.5 and \$5 bn hedge fund RAUM
  - April 30, 2013 – more than \$1.5 bn in private equity fund RAUM & all advisers with between \$150 mn and \$1.5 bn of private fund RAUM
    - *(Note: \$5 bn threshold is irrelevant for private equity fund advisers with calendar fiscal year)*
- Initial filings must be complete (i.e., non-hedge fund private funds cannot be omitted until a later filing, although this does apply for subsequent updating requirements).

# Poll Question 1

- Have you reviewed and/or made modifications to your fund subscription documents in order to collect information required for Form PF reporting?
  - A. Yes
  - B. No

# Poll Question 2

- Are you using any third-party services to assist with data management and Form PF reporting?
  - A. Yes
  - B. No

# Poll Question 3

- Has your organization restructured its related advisers or client accounts or passed on business opportunities in an attempt to remain within a certain Form PF classification?
  - A. Yes
  - B. No

# Form PF – Commodity Pools

- Do commodity pools need to be included in the initial Form PF filing?
  - Is the commodity pool a “private fund”?
    - *If yes, then must be included in initial filing.*
  - If no, then is the adviser registered as a CPO or CTA?
    - *If no, then may be filed voluntarily, even if the pool is not a “private fund” (i.e., does not rely on 3(c)(1) or 3(c)(7)).*
    - *If yes, then filing is only required under the CFTC reporting regime (i.e., Forms CPO-PQR and CTA-PR) after September 2012, which is the effective date of CFTC Rule 4.27(d) for \$5 billion asset CPOs/CTAs (Dec. 14, 2012 otherwise)).*
    - *Note: CFTC Rule 4.13(a)(4), which is currently heavily relied on by 3(c)(7) funds, will not exist after December 31, 2012, so many advisers and sub-advisers will likely have to register as CPOs and/or CTAs, which will trigger application of Rule 4.27(d), which may require that non-private fund commodity pools be included in future Form PF filings.*

# Form PF – Fund of Funds

- For determining classification, advisers need not calculate private fund assets invested in the equity of other private funds.
- Funds that only invest in equity of other private funds, cash, cash equivalents and currency hedging instruments need only be reported on Section 1(b).
  - The SEC has indicated that this treatment is the same for private funds that invest in the equity of other private funds whether or not the filing adviser serves as adviser for the invested private funds.
- Advisers solely to such “disregarded private funds” must report on Form PF if the \$150 million threshold is met, although such an adviser would not have to report beyond Section 1.

# Form PF – Affiliates and Sub-Advisers

- Advisers and related persons may report on a single Form PF.
  - The SEC is upgrading the reporting system to permit relying advisers or special purpose vehicles (SPVs) without filing numbers to be listed.
  - Until then, the SEC has advised such entities should be identified in Question 4.
- Sub-advisers: Fund information should only be reported once.
  - Must coordinate with one another.
  - The adviser that reports Section 7.B.1. of Schedule D to Form ADV should be the adviser that reports on Form PF.
  - If such ADV-reporting adviser is not required to file Form PF, then the other adviser should report.



# Form PF – International Implications

- Advisers *may* treat non-US funds as “private funds” if they would be private funds if they used US jurisdictional means in offering their shares.
- Adviser with a principal office and place of business outside the US may exclude private funds that are not “US Persons,” offered in the US or beneficially owned by any US Person.

# Form PF – Reportable Information

- Section 1 - Required disclosure for all Form PF reporters:
  - Section 1(a):
    - *Identifying information about the adviser (including reporting related persons);*
    - *Large trader ID (if any);*
    - *Aggregate RAUM and net assets per private fund category; and*
    - *“Miscellaneous” – assumptions made in reporting.*

# Form PF – Reportable Information

- Section 1 - Required disclosure for all Form PF reporters:
  - Section 1(b):
    - *Identifying information about each private fund;*
      - Single 1(b) permissible for master-feeders or parallel funds.
    - *Gross and net asset value;*
    - *Investment in other private funds;*
    - *Borrowings and creditors (i.e., US or foreign, financial or non-financial institutions);*
    - *Outstanding derivatives positions;*
    - *Level 1, 2 and 3 and cost-based assets and liabilities;*
    - *Concentration among five largest beneficial owners;*
    - *Ownership of fund equity across investor types; and*
      - Good faith estimates permissible for interests outstanding prior to March 31, 2012.
    - *Fund performance on both gross basis and net of fees and allocations basis.*
      - Consistent with method reported to investors or used internally.
      - Annual performance required.
      - Quarterly and monthly performance only required if already being calculated , size, leverage, performance.

# Form PF – Reportable Information

- Section 1 - Required disclosure for all Form PF reporters:
  - Section 1(c):
    - *Information about each hedge fund;*
    - *Single or multiple investment strategies?*
    - *Percentage of fund net asset value allocated to strategies;*
    - *Percentage of fund net asset value using high-frequency trading strategies;*
    - *Five largest counterparty exposures; give counterparties with largest exposure to fund;*
    - *Trading and clearing practices; and*
    - *Activities outside the securities and derivatives markets.*

# Form PF – Reportable Information

- Section 2 - Required disclosure for large advisers to hedge funds (i.e., \$1.5 bn in hedge fund RAUM):
  - Section 2(a): Aggregate hedge fund information:
    - *Value of assets invested in different types of securities and commodities on both a short and long basis;*
    - *Must report duration, weighted average tenor or 10-year bond equivalent for fixed income holdings;*
    - *Transaction value of monthly turnover in asset classes (indicative of trade frequency and market liquidity attributable to hedge funds); and*
    - *Geographical breakdown of investments (regional and particular countries of interest (BRIC, Japan, US)).*

# Form PF – Reportable Information

- Section 2 - Required disclosure for large advisers to hedge funds (i.e., \$1.5 bn in hedge fund RAUM):
  - Section 2(b): Hedge-fund specific information (only for “qualifying” hedge funds: \$500 mm aggregate net asset value at the end of any month during prior fiscal quarter)
    - *Single 2(b) permissible for master-feeders or parallel funds;*
    - *Fund identifying information;*
    - *Question 30 parallels Question 26, but on a fund-specific basis;*
    - *Portfolio liquidity;*
    - *Value of “unencumbered cash” (cash, cash equivalents and overnight repos, excluding that transferred as collateral or subject to a security interest, lien or other encumbrance);*
    - *Concentration;*
    - *Collateral practices with counterparties; and*
    - *Whether any trades were cleared directly through a central clearing counterparty (CCP).*

# Form PF – Reportable Information

- Section 2 - Required disclosure for large advisers to hedge funds (i.e., \$1.5 bn in hedge fund RAUM):
  - Section 2(b): Hedge-fund specific information (only for “qualifying” hedge funds: \$500 mm aggregate net asset value at the end of any month during prior fiscal quarter)
    - *Monthly Value at Risk (VaR), if regularly calculated*
    - *Portfolio impact from identified market factors*
      - *May omit responses to market factors not regularly considered in formal testing*
    - *Secured and unsecured borrowing*
    - *Value of collateral, credit support and types of creditors*
    - *Total notional derivatives exposures*
    - *Net mark-to-market value of uncleared derivatives positions and value of related collateral and other credit support posted*
    - *Available financing and identify of and amounts owed to creditors*
    - *Investors composition and liquidity*
      - *Side pockets and gating arrangements*

# Form PF – Reportable Information

- Section 3 - Required disclosure for large advisers to liquidity funds (i.e., \$1 bn in liquidity fund RAUM):
  - Identifying information
  - Portfolio valuation and methodology
  - Liquidity
  - Exposures and investor concentration and liquidity



# Form PF – Reportable Information

- Section 4 - Required disclosure for large advisers to private equity funds (i.e., \$2 bn in private equity fund RAUM):
  - Information on underlying portfolio companies, including leverage
  - Debt-to-equity ratios and gross asset values of portfolio companies
  - Investments broken down by industry and geography

# Form PF – Reporting Clarifications from SEC FAQs

- The SEC has indicated that filers can provide assumptions made in their reports in response to Question 4.
- Exchange-traded futures contracts entered into through an FCM that is a clearing member of the exchange are “derivatives” on a “regulated exchange or swap execution facility” and “cleared by a central counterparty clearinghouse” for purposes of Question 24, although not directly cleared for purposes of Question 39.

# Form PF – Reporting Clarifications from SEC FAQs

- “Listed equity derivatives” refers to a fund’s exposure to derivatives for which the underlying asset is listed equities.
- Fund positions that could be classified under multiple sub-asset classes should be included in the sub-asset class that best describes the position with the highest degree of precision.
- Geographical reporting is flexible and may reflect internal methodologies and investor reporting.
  - These may also be noted in response to Question 4.

# Form PF - Confidentiality

- Form PF filings will be subject to filing fees.
- Although information submitted on Form PF is nonpublic and not subject to FOIA requests, the SEC may use the information in enforcement actions and it may be accessed by various federal departments and agencies, including FSOC and the CFTC, and by self-regulatory organizations within the scope of their jurisdiction.
- The SEC indicated that it will implement substantial safeguards to protect the confidentiality of information.
- Form PF will be submitted electronically to a system designed and hosted by the Financial Industry Regulatory Authority (FINRA), similar to the IARD system.

# Form PF - Planning

- What you should be doing:
  - Review your structure and determine your status and subsequent reporting requirements (both deadlines and scope)
  - Determine whether account or corporate reorganizations would be beneficial in terms of increasing reporting efficiencies
  - Begin reviewing Form PF now to ensure that your systems are appropriately designed to capture necessary information as your applicable deadline(s) approach
  - Put together a chart/matrix specific to your firm that identifies: (1) required data, (2) frequency of reporting, and (3) source of data
  - Establish contacts with necessary third parties (i.e., prime brokers, administrators, pricing vendors, custodians) to set up reporting lines
  - Organize compliance team with clear tasks and assignments
  - Plan a “dry run” two weeks in advance of initial filing, if possible, and make any tweaks to system that are identified to catch what’s “falling through”
  - Determine which of your portfolio holdings are hard to classify or that slip through your system
  - Internal tools created for Form PF compliance must be designed to fit together with BOTH your firm and Form PF

# Form PF

Questions?

# Treasury International Capital (“TIC”) Reporting Requirements

# Treasury International Capital (“TIC”)

- Overview TIC Reporting System
  - Used to collect information regarding U.S. external claims and liabilities
  - Monthly and Quarterly Reports
    - *B Forms (filed by banks and broker-dealers)*
    - *C Forms (filed by nonbank organizations)*
    - *Form D (filed by derivatives markets participants)*
    - *Form S (filed by sellers and purchasers or long-term securities)*
    - *Form SLT (filed by those engaged in cross-border holdings of long-term securities)*
  - Annual and Benchmark Reports
    - *Forms SHC and SHCA (U.S. ownership of foreign securities)*
    - *Forms SHL and SHLA (foreign residents’ holdings of U.S. securities)*



# Form S

- Reportable transactions
  - Purchases or sales of equity securities or debt securities with a maturity greater than one year that are undertaken directly with foreign residents
  - Transactions between U.S. funds and their foreign affiliates are generally reportable transactions

# Form SLT

- Approved by the Office of Management and Budget in June 2011
- U.S. private funds that sell interests to non-U.S. investors or invest in non-U.S. securities may need to report on Form SLT if the aggregate value of interests sold AND securities purchased exceeds \$1 billion
  - Interests in excess of 10% voting securities are excluded
  - Securities purchased and held through a U.S. resident custodian are excluded
- No reporting required for non-U.S. private funds

# Form SLT

- Report due to Federal Reserve by 23<sup>rd</sup> calendar day following the last day of the month during which a reporting requirement is triggered
- Individual information is kept confidential by Treasury; aggregate data is publicly available
- Possible reporting entities:
  - U.S. custodians that hold U.S. securities for foreign residents or foreign securities for U.S. residents
  - U.S. issuers of securities that are held directly or owned by foreign residents
  - U.S. investors that directly hold foreign securities
- Residency is determined based on legal jurisdiction and not actual location

# Form SLT

- Filing Thresholds
  - Once \$1 billion threshold is met, Form SLT must be filed for every subsequent month of the calendar year, even if holdings fall below \$1 billion
  - Issued securities and reportable long-term securities invested in must be aggregated
- Reportable Information
  - Fair market value of securities issued to non-U.S. residents, country of residence and whether such investor is a “Foreign Official Institution” (i.e., foreign treasury or bank that is financial agent of foreign government)
  - Fair market value of foreign securities held, country of residence and whether such securities are foreign government bonds, corporate bonds or equity



## international presence

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