PUBLICATION

SEC Amendments Require Advisers to Disclose More Information and Keep Additional Records

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On August 25, 2016, the Securities and Exchange Commission (SEC) adopted amendments to Form ADV and to several rules under the Investment Advisers Act of 1940 (Advisers Act) (collectively, the Amendments). The Adopting Release is here. The SEC adopted the Amendments to require additional information from advisers that will allow investors and the SEC to better understand the risk profile of individual advisers and the industry as a whole. As addressed in more detail below, the Amendments to Form ADV will, among other things, (1) require additional disclosures regarding separately managed accounts (SMAs), (2) require advisers to disclose additional information about their advisory business, including information about their branch office operations and use of social media, and (3) permit "umbrella registration," which is a method for private fund adviser entities operating a single advisory business to register with the SEC using one Form ADV. The Amendments to Rule 204-2 of the Advisers Act (the books and records rule) will require advisers to maintain additional records regarding performance calculations and communications.

The Amendments become effective 60 days after publication in the Federal Register, and advisers will need to be in compliance with the Amendments by October 1, 2017.

Amendments to Form ADV:

The noteworthy Amendments to Part 1A of Form ADV involve three areas: (1) revisions to fill certain data gaps and to provide additional information about investment advisers, including their SMA business; (2) revisions requiring advisers to disclose additional information about their operations; and (3) amendments to incorporate umbrella registrations currently outlined in staff guidance. These three areas are addressed in more detail below. The amended Form ADV is here.

(1) Additional Disclosures Related to SMAs

A substantial majority of SEC-registered investment advisers manage a wide variety of client assets in SMAs, which generally provide advisory clients with individualized investment advice and direct ownership of the securities and other assets in the account. (For purposes of reporting on Form ADV, all accounts that are not pooled investment vehicles – i.e., registered investment companies, business development companies and other pooled investment vehicles such as private funds – are SMAs.) Currently, Item 5 to Part 1A of Form ADV requires advisers to disclose only limited information about their SMAs (e.g., percentage of clients that are separately managed accounts and percentage of regulatory assets under management that represent separately managed accounts). The Amendments require advisers to provide increased information on SMAs by adding questions in Item 5 to Part 1A and Section 5 of Schedule D with respect to the following:

- **Asset Categories:** Advisers will be required to report the approximate percentage of their SMA regulatory assets under management (RAUM) invested in 12 different asset categories: exchange traded equity securities; non-exchange traded equity securities; U.S. government bonds; U.S. state and local bonds; sovereign bonds; investment grade corporate bonds; non-investment grade corporate bonds; derivatives; securities issued by registered investment companies and business

development companies; securities issued by other pooled investment vehicles; cash and cash equivalents; and "other." Advisers may use their own methodologies in determining appropriate asset categories. Advisers with at least $10 billion in RAUM attributable to SMAs must report this information on an annual basis with respect to the percentages as of mid-year and year-end. Advisers with less than $10 billion in RAUM attributable to SMAs also must report this information on an annual basis, but only with respect to the year-end percentages.

- **Borrowings and Derivatives:** Advisers will be required to report information regarding the use of borrowings and derivatives in any SMA with RAUM of at least $10 million. Advisers with RAUM attributable to SMAs of between $500 million and $10 billion must report the amount RAUM attributable to SMAs and the dollar amount of borrowings attributable to those assets that correspond to three levels of gross notional exposures. Advisers with RAUM attributable to SMAs of at least $10 billion must report the same information as well as the derivative exposures across six different categories of derivatives. Notably, all advisers to SMAs will be required to report the percentage of SMA assets held in derivatives.
- **Custodians:** Advisers will be required to identify any custodian (including office location) that accounts for at least ten percent of total RAUM attributable to SMAs. For each such custodian, advisers must disclose the amount of RAUM held at such custodian.

(2) Additional Disclosures Related to Operations of Advisory Business

The Amendments require investment advisers to disclose the following additional information, among other new information, on Form ADV:

- **Social Media:** The Amendments will now require an adviser to identify all accounts on social media platforms (e.g., Twitter, Facebook, LinkedIn) in which they control the content and to provide the address of each of the adviser's social media pages. Advisers must also continue reporting the address of each of their websites.
- **Office Locations:** Advisers will be required to provide the total number of offices in which they conduct business as well as information about their 25 largest offices, based on the number of personnel. The information required to be disclosed includes each office's CRD branch number (if applicable), the number of employees performing advisory functions from such office, the identity from a categorical list of securities related activities that are conducted from such office and a narrative description of any other investment-related business conducted from such office.
- **Chief Compliance Officer:** In addition to the name and contact information of an adviser's chief compliance officer (CCO), investment advisers will be required to confirm whether the CCO is employed by someone other than the adviser or a related person of the adviser (unless the CCO's employer is a registered investment company advised by the investment adviser). If the CCO is employed by someone other than the adviser or a related person of the adviser, the name and EIN of that employer must be disclosed.

(3) Umbrella Registration

The Amendments will provide a more efficient method for the registration on one Form ADV of multiple private fund adviser entities operating a single advisory business ("umbrella registration"). The SEC issued no-action guidance to private fund advisers in 2012 with respect to umbrella registration. The Amendments incorporating umbrella registration into Form ADV are intended to make the availability of umbrella registration more widely known to advisers. According to the SEC, uniform filing requirements for umbrella registration in Form ADV will provide more consistent data about, and create a clearer picture of, groups of private fund advisers that operate as a single business. The Amendments update Form ADV's General Instructions and establish five

conditions that the private fund advisers must satisfy to be eligible for umbrella registration. Notably, umbrella registration is not mandatory, and does not extend to non-U.S. advisers or to exempt reporting advisers.

Amendments to Rule 204-2 (Books & Records Rule) of the Advisers Act:

The Amendments will require investment advisers to maintain additional books and records relating to the calculation and distribution of performance information:

- Specifically, advisers will be required to maintain the materials listed in Rule 204-2(a)(16) that demonstrate the calculation of the performance or rate of return in any communication that the adviser circulates or distributes, directly or indirectly, to any person. Before the Amendments, advisers were only required to maintain materials supporting performance claims that were distributed to ten or more persons.
- The Amendments also amend Rule 204-2(a)(7) to require advisers to maintain originals of all written communications received and copies of written communications sent by an investment adviser relating to the performance or rate of return of any or all managed accounts or securities recommendations. Such communications must be maintained regardless of whether they are personalized client communications or an advertisement sent to multiple persons.

If you have questions or would like to learn more about the Amendments addressed in this Alert, or any other securities-related issues, please contact one of the attorneys in Baker Donelson's Broker-Dealer/Registered Investment Adviser group.