

114TH CONGRESS  
2D SESSION

# H. R. 5424

To amend the Investment Advisers Act of 1940 and to direct the Securities and Exchange Commission to amend its rules to modernize certain requirements relating to investment advisers, and for other purposes.

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## IN THE HOUSE OF REPRESENTATIVES

JUNE 9, 2016

Mr. HURT of Virginia (for himself, Mr. VARGAS, Mr. FOSTER, and Mr. STIVERS) introduced the following bill; which was referred to the Committee on Financial Services

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## A BILL

To amend the Investment Advisers Act of 1940 and to direct the Securities and Exchange Commission to amend its rules to modernize certain requirements relating to investment advisers, and for other purposes.

1 *Be it enacted by the Senate and House of Representa-*  
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE.**

4 This Act may be cited as the “Investment Advisers  
5 Modernization Act of 2016”.

1 **SEC. 2. MODERNIZING CERTAIN REQUIREMENTS RELATING**  
2 **TO INVESTMENT ADVISERS.**

3 (a) MAINTENANCE OF BOOKS AND RECORDS.—Not  
4 later than 90 days after the date of the enactment of this  
5 Act, the Securities and Exchange Commission shall amend  
6 section 275.204–2 of title 17, Code of Federal Regula-  
7 tions, to provide that an investment adviser is not required  
8 to maintain—

9 (1) any communications or materials (including  
10 communications or materials made available in a se-  
11 cure electronic or physical data room) used in con-  
12 nection with due diligence for a prospective invest-  
13 ment, if the communications or materials are subject  
14 to a confidentiality agreement; or

15 (2) any written communications required by  
16 paragraph (a)(7) of such section, if the communica-  
17 tions are sent and received only by supervised per-  
18 sons of the investment adviser.

19 (b) INVESTMENT ADVISORY CONTRACTS.—

20 (1) ASSIGNMENT.—

21 (A) ASSIGNMENT DEFINED.—Section  
22 202(a)(1) of the Investment Advisers Act of  
23 1940 (15 U.S.C. 80b–2(a)(1)) is amended by  
24 striking “; but” and all that follows and insert-  
25 ing “; but no assignment of an investment advi-  
26 sory contract shall be deemed to result from the

1 death or withdrawal, or the sale or transfer of  
2 the interests, of a minority of the members,  
3 partners, shareholders, or other equity owners  
4 of the investment adviser having only a minor-  
5 ity interest in the business of the investment  
6 adviser, or from the admission to the invest-  
7 ment adviser of one or more members, partners,  
8 shareholders, or other equity owners who, after  
9 such admission, shall be only a minority of the  
10 members, partners, shareholders, or other eq-  
11 uity owners and shall have only a minority in-  
12 terest in the business.”.

13 (B) CONSENT TO ASSIGNMENT BY QUALI-  
14 FIED CLIENTS.—Section 205(a)(2) of the In-  
15 vestment Advisers Act of 1940 (15 U.S.C. 80b-  
16 5(a)(2)) is amended by inserting before the  
17 semicolon the following: “, except that if such  
18 other party is a qualified client (as defined in  
19 section 275.205-3 of title 17, Code of Federal  
20 Regulations, or any successor thereto), such  
21 other party may provide such consent at the  
22 time the parties enter into, extend, or renew  
23 such contract”.

24 (2) NOT REQUIRED TO PROVIDE FOR NOTIFICA-  
25 TION OF CHANGE IN MEMBERSHIP OF PARTNER-

1 SHIP.—Section 205 of the Investment Advisers Act  
2 of 1940 (15 U.S.C. 80b–5) is amended—

3 (A) in subsection (a)—

4 (i) in paragraph (1), by striking the  
5 semicolon and inserting “; or”;

6 (ii) in paragraph (2), by striking “;  
7 or” and inserting a period; and

8 (iii) by striking paragraph (3); and

9 (B) in subsection (d), by striking “para-  
10 graphs (2) and (3) of subsection (a)” and in-  
11 serting “subsection (a)(2)”.

12 (c) ADVERTISING RULE.—

13 (1) IN GENERAL.—Not later than 90 days after  
14 the date of the enactment of this Act, the Commis-  
15 sion shall amend section 275.206(4)–1 of title 17,  
16 Code of Federal Regulations, to provide that para-  
17 graphs (a)(1) and (a)(2) of such section do not  
18 apply to an advertisement that an investment ad-  
19 viser publishes, circulates, or distributes solely to  
20 persons described in paragraph (2) of this sub-  
21 section.

22 (2) PERSONS DESCRIBED.—A person is de-  
23 scribed in this paragraph if such person is, or the  
24 investment adviser reasonably believes such person  
25 is—

1 (A) a qualified client (as defined in section  
2 275.205–3 of title 17, Code of Federal Regula-  
3 tions), determined as of the time of the publica-  
4 tion, circulation, or distribution of the adver-  
5 tisement rather than immediately prior to or  
6 after entering into the investment advisory con-  
7 tract referred to in such section;

8 (B) a knowledgeable employee (as defined  
9 in section 270.3c–5 of title 17, Code of Federal  
10 Regulations) of any private fund to which the  
11 investment adviser acts as an investment ad-  
12 viser;

13 (C) a qualified purchaser (as defined in  
14 section 2(a) of the Investment Company Act of  
15 1940 (15 U.S.C. 80a–2(a))); or

16 (D) an accredited investor (as defined in  
17 section 230.501 of title 17, Code of Federal  
18 Regulations), determined as if the investment  
19 adviser were the issuer of securities referred to  
20 in such section and the time of the publication,  
21 circulation, or distribution of the advertisement  
22 were the sale of such securities.

1 **SEC. 3. REMOVING DUPLICATIVE BURDENS AND APPRO-**  
2 **PRIATELY TAILORING CERTAIN REQUIRE-**  
3 **MENTS.**

4 (a) **BROCHURE DELIVERY.**—Not later than 90 days  
5 after the date of the enactment of this Act, the Commis-  
6 sion shall amend section 275.204–3(c) of title 17, Code  
7 of Federal Regulations, to provide that an investment ad-  
8 viser is not required to deliver a brochure or brochure sup-  
9 plement to a client that is a limited partnership, limited  
10 liability company, or other pooled investment vehicle for  
11 which each limited partner, member, or other equity owner  
12 has received, before purchasing a security issued by the  
13 pooled investment vehicle, a prospectus, private placement  
14 memorandum, or other offering document containing (to  
15 the extent material to an understanding of the pooled in-  
16 vestment vehicle, the business of the pooled investment ve-  
17 hicle, and the securities being offered by the pooled invest-  
18 ment vehicle) substantially the same information as would  
19 be required by Part 2A or 2B of Form ADV at the time  
20 of delivery of the brochure or brochure supplement, as the  
21 case may be.

22 (b) **FORM PF.**—Not later than 90 days after the date  
23 of the enactment of this Act, the Commission shall amend  
24 section 275.204(b)–1 of title 17, Code of Federal Regula-  
25 tions, to provide that an investment adviser to a private  
26 fund is not required to report any information beyond that

1 which is required by sections 1a and 1b of Form PF, un-  
2 less such investment adviser is a large hedge fund adviser  
3 or a large liquidity fund adviser (as such terms are defined  
4 in such Form).

5 (c) FREQUENCY OF TRANSACTION REPORTS BY AC-  
6 CESS PERSONS.—Not later than 90 days after the date  
7 of the enactment of this Act, the Commission shall amend  
8 section 275.204A–1 of title 17, Code of Federal Regula-  
9 tions, so as to provide that, in the case of an investment  
10 adviser that acts as an investment adviser solely to one  
11 or more clients that primarily own or hold securities that  
12 are not public securities (regardless of whether such secu-  
13 rities were public securities at the time of acquisition by  
14 the client or clients), the code of ethics required by such  
15 section shall require the access persons of the investment  
16 adviser to submit the transaction reports described in  
17 paragraph (b)(2) of such section at a frequency specified  
18 by the investment adviser, but not less frequently than an-  
19 nually.

20 (d) CUSTODY RULE.—Not later than 90 days after  
21 the date of the enactment of this Act, the Commission  
22 shall amend section 275.206(4)–2 of title 17, Code of Fed-  
23 eral Regulations, as follows:

24 (1) The Commission shall provide additional ex-  
25 ceptions to the independent verification requirement

1 of paragraph (a)(4) of such section for an invest-  
2 ment adviser with respect to funds and securities of  
3 a limited partnership (or a limited liability company  
4 or other type of pooled investment vehicle), as fol-  
5 lows:

6 (A) An exception that applies if the out-  
7 standing securities (other than short-term  
8 paper, as defined in section 2(a) of the Invest-  
9 ment Company Act of 1940 (15 U.S.C. 80a-  
10 2(a))) of the pooled investment vehicle are ben-  
11 efiticially owned exclusively by—

12 (i) the investment adviser;

13 (ii) affiliated persons of the invest-  
14 ment adviser;

15 (iii) supervised persons of the invest-  
16 ment adviser;

17 (iv) officers, directors, and employees  
18 of the affiliated persons of the investment  
19 adviser;

20 (v) family members and former family  
21 members (as such terms are defined in sec-  
22 tion 275.202(a)(11)(G)–1 of title 17, Code  
23 of Federal Regulations) of persons de-  
24 scribed in clause (iii) or (iv); or



1 (vi) officers, directors, employees, or  
2 affiliated persons of, or persons who pro-  
3 vide, have provided, or have entered into a  
4 contract to provide services to—

5 (I) the investment adviser of the  
6 pooled investment vehicle;

7 (II) one or more clients of the in-  
8 vestment adviser of the pooled invest-  
9 ment vehicle; or

10 (III) issuers from which the  
11 pooled investment vehicle or any other  
12 client of the investment adviser of the  
13 pooled investment vehicle has acquired  
14 securities, such as the portfolio com-  
15 pany of a private fund.

16 (B) An exception that applies if the pooled  
17 investment vehicle has been established to hold  
18 only the securities of a single issuer in which  
19 one or more pooled investment vehicles man-  
20 aged by the investment adviser have acquired a  
21 controlling interest.

22 (2) Consistent with, and expanding on, IM  
23 Guidance Update No. 2013–04, titled “Privately Of-  
24 fered Securities under the Investment Advisers Act  
25 Custody Rule”, published by the Division of Invest-

1       ment Management of the Commission, the Commis-  
2       sion shall, with respect to the exception for certain  
3       privately offered securities in paragraph (b)(2) of  
4       such section—

5               (A) remove the requirement of clause  
6               (i)(B) of such paragraph (relating to the  
7               uncertificated nature and recordation of owner-  
8               ship of the securities); and

9               (B) remove the requirement of clause (ii)  
10              of such paragraph (relating to audit and finan-  
11              cial statement distribution requirements with  
12              respect to securities of pooled investment vehi-  
13              cles).

14       (e) PROXY VOTING RULE.—Not later than 90 days  
15       after the date of the enactment of this Act, the Commis-  
16       sion shall amend section 275.206(4)–6 of title 17, Code  
17       of Federal Regulations, to provide that such section does  
18       not apply to any voting authority with respect to client  
19       securities that are not public securities.

20       **SEC. 4. FACILITATING ROBUST CAPITAL FORMATION BY**  
21                               **PREVENTING REGULATORY MISMATCH.**

22       The Commission may not—

23               (1) amend section 230.156 of title 17, Code of  
24       Federal Regulations, to extend the provisions of

1 such section to offerings of securities issued by pri-  
2 vate funds; or

3 (2) adopt rules applicable to offerings of securi-  
4 ties issued by private funds that are substantially  
5 the same as the provisions of such section.

6 **SEC. 5. EXCLUSION OF ADVISORY SERVICES TO REG-**  
7 **ISTERED INVESTMENT COMPANIES.**

8 This Act shall not apply with respect to advisory serv-  
9 ices provided, or proposed to be provided, to an investment  
10 company registered under the Investment Company Act  
11 of 1940 (15 U.S.C. 80a–1 et seq.).

12 **SEC. 6. REFERENCES TO REGULATIONS.**

13 In this Act, any reference to a regulation shall be con-  
14 strued to refer to such regulation or any successor thereto.

15 **SEC. 7. DEFINITIONS.**

16 In this Act:

17 (1) PUBLIC SECURITY.—The term “public secu-  
18 rity” means a security issued by an issuer that—

19 (A) is required to submit reports under  
20 section 13(a) or 15(d) of the Securities Ex-  
21 change Act of 1934 (15 U.S.C. 78m(a);  
22 78o(d)); or

23 (B) has a security that is listed or traded  
24 on any exchange or organized market operating  
25 in a foreign jurisdiction.

1           (2) TERMS DEFINED IN INVESTMENT ADVISERS  
2           ACT OF 1940.—The terms defined in section 202(a)  
3           of the Investment Advisers Act of 1940 (15 U.S.C.  
4           80b–2(a)) have the meanings given such terms in  
5           such section.

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