HEDGE FUND REGULATORY FRAMEWORK

Hedge funds are regulated investment vehicles designed to facilitate investment by pensions, endowments and other sophisticated investors in traditionally liquid investment opportunities. Hedge fund managers act as investment advisers to the funds they manage and generally are subject to federal and, in some cases, state laws covering their activities as investment advisers. Like other investors, hedge funds are subject to federal laws prohibiting insider trading, market manipulation, and fraud. As part of the U.S. framework for financial supervision, multiple state and federal regulators coordinate to monitor the financial services industry, protect investors, promote effective capital markets, and address issues that could pose a systemic risk to the economy.

Federal Branch Agencies Overseeing the Hedge Fund Industry

Securities and Exchange Commission (SEC)

The Securities and Exchange Commission (SEC) is the primary regulator of hedge funds and their managers.

SEC Registration

Under Title IV of the Dodd-Frank Act, managers of hedge funds with more than $110 million in total assets under management must register with and report regularly to the SEC regarding their operations, holdings, leverage, trades, and counterparty exposures. Smaller advisers are typically registered with state regulators. Specific reporting is required regarding hedge funds on Form ADV and Form PF.

Antifraud Enforcement

Hedge funds are subject to the antifraud provisions of the Securities Exchange Act of 1934 (the "Exchange Act") and SEC Rule 10b-5 thereunder, as well as the slightly broader provisions of Section 206 of the Investment Advisers Act of 1940 (the "Advisers Act"), which covers all fund managers whether registered or not. These antifraud provisions expressly prohibit market manipulation. Managers registered with the SEC as investment advisers are fiduciaries required to comply with additional requirements regarding all investor communications.

Marketing

Hedge funds are subject to private offering rules that bar marketing of fund interests to retail investors and govern required disclosures and practices related to marketing of past, hypothetical and model performance and the solicitation of investors using third-party solicitors.

Recordkeeping

The Advisers Act imposes far-reaching recordkeeping requirements on advisers to hedge funds registered with the SEC. These records must be available to the SEC for inspection.

Compliance Procedures

The Advisers Act requires hedge fund managers to maintain detailed and tailored internal policies and procedures to guard against violations of the Advisers Act and the rules and regulations promulgated thereunder. The SEC also requires advisers to have specific policies and procedures addressing operational concerns, such as business continuity, cybersecurity, and data protection. Advisers who fail to develop and abide by appropriate policies may have operational deficiencies that lead to SEC enforcement actions against the adviser.

Examination and Enforcement

The SEC has examination and enforcement authority over registered advisers and hedge funds.

Disclosures

Hedge funds and their managers are subject to disclosure requirements under the Exchange Act, including beneficial ownership reports and quarterly holdings reports.

Federal Branch Agencies Overseeing the Hedge Fund Industry

Commodity Futures Trading Commission (CFTC)

The Commodity Futures Trading Commission (CFTC) is an independent federal agency that regulates, together with the SEC, many aspects of the derivatives market. It protects market users and the public from fraud, manipulation, and abusive practices in the sale of commodity and financial futures and options, and fosters open, competitive option markets.

CFTC Registration

Hedge fund managers that trade a certain amount of derivatives generally must register with the CFTC as a commodity pool operator ("CPO") or commodity trading advisor ("CTA"). Registered CPOs and CTAs are subject to numerous regulatory requirements, including extensive investor disclosure and reporting, recordkeeping, advertising restrictions and antifraud requirements. Certain hedge funds rely on exemptions from being classified as CPOs, and may renew those relevant exemptions with the CFTC and the National Futures Association ("NFA") on an annual basis. Specific reporting is required from hedge funds on Form CPO-PQR.

Disclosure

CFTC requires specific information to be disclosed to investors, including prescribed risk and performance disclosures, and for funds to maintain supervisory and training standards for employees.

Safeguards on Customer Accounts

CPOs are required to prepare and distribute internal and periodic reports to pool participants, including annual reports that are prepared in accordance with GAAP. In addition, CPOs are prohibited from comingling the assets of a pool that it operates with the assets of any other person. CTAs generally are prohibited from soliciting or accepting client funds to purchase, margin, guarantee or secure any commodity interest of the client.

Derivatives

Major market participants trading in derivatives, including hedge funds, are subject to margin and clearing requirements to limit counterparty and systemic risk. Market participants are also subject to position limits.

Financial Stability Oversight Council (FSOC)

The Financial Stability Oversight Council (FSOC) is a council of regulators established by the Dodd-Frank Act. The Council (1) monitors systemic risks to the U.S. financial system; (2) eliminates expectations that any American financial firm is "too big to fail;" (3) coordinates regulatory reporting and rulemaking; and (4) responds to emerging threats to U.S. financial stability. FSOC can also make recommendations to financial regulatory agencies to apply new or heightened standards and safeguards for financial activities or practices that could create risk to U.S. financial stability. The Treasury Secretary chairs FSOC.

Board of Governors of the Federal Reserve System (FRB)

The Board of Governors of the Federal Reserve System (FRB), serves as the central banking system. The FRB oversees monetary policy, regulates the banking system and monitors systemic risk in the financial markets. The FRB is the regulator tasked with enforcing the enhanced regulatory framework governing systemically important financial institutions and setting margin requirements for securities.

Federal Trade Commission

The Federal Trade Commission is an independent agency charged with policing unfair, deceptive or fraudulent practices in the marketplace and enforcing antitrust laws to promote competitive markets. Among its tools to address competition concerns is the Hart-Scott-Rodino Act (HSR), which established a federal premerger notification program that provides the FTC and the Department of Justice with information about large mergers and acquisitions before they occur. Under HSR, acquisitions of stock in excess of a certain dollar threshold and percentage of an issuers voting shares must be first reported unless an exemption applies. This filing requirement sometimes applies to acquisitions of stock made by hedge funds.

Self-Regulatory Organizations (SROs)

National Futures Association (NFA)

The National Futures Association (NFA) is a self-regulatory organization ("SRO") that regulates the managed futures industry, including hedge funds that are CPOs. Membership in NFA is mandatory for the more than 4,200 firms and 55,000 individuals trading in the marketplace NFA regulates industry participants through: registration; annual reporting and disclosure; examinations; monitoring for market manipulation and systemic risk; and enforcement mechanisms to address potential manipulation.

Financial Industry Regulatory Authority (FINRA)

The Financial Industry Regulatory Authority (FINRA) is an SRO for broker-dealers and certain stock exchanges. FINRA regulates and examines broker-dealer firms and their registered personnel. FINRA also regulates sales of hedge fund interests to investors through broker-dealers.

State Regulatory Agencies

Each state has financial services regulators who oversee financial services markets and participants to the extent not preempted by federal law. Additionally, many state attorneys general have oversight authority, including general antifraud authority.

Hedge fund managers with less than $110 million in assets under management or that are not otherwise subject to regulation by the SEC generally are required to register with the state securities commissioners in the jurisdictions in which they are headquartered or operate. Personnel affiliated with hedge fund managers and certain solicitors also may be required to register individually with state regulatory agencies as investment adviser representatives. In addition, certain states impose substantive reporting and compliance requirements on hedge fund managers registered with the state that mirror – or in some cases expand upon – requirements applicable to SEC-registered investment advisers under the Advisers Act.