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SEC Finalizes Second Set of Form PF Updates

On February 8, 2024, the SEC and the Commodity Futures Trading Commission (CFTC) jointly adopted a second set of Form PF amendments that covers private funds, commodity pool operators (CPOs), and commodity trading advisers (CTAs). The rule passed largely as proposed. This article highlights the most noteworthy changes, which will impact all Form PF filers and include significantly more details for hedge funds and large hedge fund advisers.

These changes are in addition to Form PF changes issued in May 2023 (see our article, "SEC Finalizes First Round of Form PF Updates").

Federal Register Publication

Compliance & Effective Date
1 year after Federal Register publication

Background

Form PF, adopted by the SEC and the CFTC in 2011, provides the SEC and the Financial Stability Oversight Council with confidential information on basic operations and strategies of private funds to monitor and assess systemic risk. Private funds are pooled investment vehicles excluded from the definition of "investment company" under the *Investment Company Act of 1940*. An adviser must file Form PF if:

- It is registered or required to register with the SEC as an investment adviser.
- It manages one or more private funds.
- The adviser and its related persons have at least $150 million in private fund assets under management (AUM) as of the last day of its most recently completed fiscal year.

A CPO or CTA that also is registered or required to register with the SEC as an investment adviser and satisfies the three conditions above must file Form PF for any commodity pool it manages that is a private fund.

See the Appendix for a summary of Form PF filing requirements.

Scope & Market Size

These changes would apply to all categories of private fund advisers, including—but not limited to—advisers to hedge funds, private equity (PE) funds, real estate funds, securitized asset funds, liquidity funds, and venture capital funds. Some recent first quarter 2023 market statistics based on reporting on Form PF include:

- **Hedge funds**. There were 9,846 hedge funds—managed by 1,856 advisers—with almost $9.5 trillion in gross AUM, which represented almost half of the gross assets reported by private fund advisers.
- **PE funds**. There were 20,917 PE funds—managed by 1,755 advisers—with $6.6 trillion in gross AUM, which represented almost one-third of the reported gross assets in the private fund industry.
- **Remaining funds**. The remaining fund categories (real estate, securitized asset, liquidity, venture capital, and other private funds) had investment discretion over almost $4.4 trillion in gross AUM managed by 1,709 fund advisers in 16,668 funds.

All Form PF Filers (General Instructions & Section 1a & 1b)

General Instructions

Complex Structures

Master-Feeder Arrangements

Private funds use complex structures, including master-feeder arrangements[1] and parallel fund structures.[2] The amendments will require advisers to report separately each component fund of a master-feeder arrangement and parallel fund structure. Currently, advisers are permitted to report either in the aggregate or separately if done consistently throughout Form PF. Aggregation would still be permitted to determine if an adviser meets a reporting threshold. Currently, advisers are not required—but have the option—to "look through" a fund's investments in any other entity (including other private funds). The final rule now standardizes reporting.

> If an adviser cannot avoid "looking through" to the reporting fund's investments in internal private funds or external private funds in responding to a particular question, then the adviser must provide an explanation.

The final rule provides an exception for a feeder fund that invests all its assets in a single master fund, U.S. treasury bills, and/or cash and cash equivalents. For these disregarded feeder funds, an adviser would look through to the applicable master fund and separate reporting is not required.

In response to comment letter feedback, the final rule clarifies a feeder fund should disregard any of its holdings in the master fund's equity when determining its reporting threshold to avoid a double counting of reported assets.

The SEC declined to provide an exception from disaggregation for PE funds while acknowledging that disaggregated reporting could be a challenge for PE fund advisers and that PE funds have a difference risk profile that hedge funds.

Funds of Funds

Currently, advisers include the value of private fund investments in other private funds in determining whether the adviser meets the Form PF filing threshold, reporting as a large hedge fund adviser, large liquidity fund adviser, or large PE fund adviser, and whether a hedge fund is a qualifying hedge fund. This requirement is implicit in the current form, and the amendments will now make this explicit.

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[1] A master-feeder arrangement is an arrangement in which one or more funds (feeder funds) invest all or substantially all their assets in a single private fund (master fund).
[2] A parallel fund structure is a structure in which one or more private funds (each, a parallel fund) pursues substantially the same investment objective and strategy and invests side by side in substantially the same positions as another private fund.

Trading Vehicles

Some private funds wholly or partially own separate legal entities that hold assets, incur leverage, or conduct trading or other activities as part of the private fund's investment activities, but do not operate a business. Private funds may use trading vehicles for various purposes—tax, regulatory or bankruptcy. Currently, Form PF does not require advisers to identify trading vehicles. Advisers will now be required to identify any trading vehicles of the reporting fund (whether wholly or partially owned), how the reporting fund uses the trading vehicle, and the fund's position sizes and counterparty exposures that are attributable to the trading vehicle.

Reporting Timelines

Large hedge fund advisers and **large liquidity fund advisers** now must update Form PF within 60 and 15 days respectively after each **calendar quarter** (deadline is currently on a **fiscal quarter** basis). All other advisers will continue to file annual updates within 120 calendar days after the end of their **fiscal year**.

Form PF will continue to require all advisers to use fiscal quarters and years to determine filing thresholds consistent with calculations in Form ADV.

Basic Information – §1a & §1b

Additional changes—not highlighted below—include clarifications on legal entity identifiers (LEIs), type of private fund, and assumptions used. Advisers must now report the date the fair value hierarchy was performed, and government securities must be broken out from cash and cash equivalents and reported separately. "Borrowings" is clarified to explicitly include synthetic long positions. All advisers must now identify the base currency of all reporting funds (currently this applies only to large hedge funds).

AUM. Advisers who file quarterly updates (large hedge fund advisers and large liquidity fund advisers) would be required to report gross asset value and net asset value (NAV) for each month of the reporting period, rather than only quarter-end data. The value of unfunded commitments included in the gross and NAVs also is required. In a change from the proposal, an adviser may report a fund's gross reporting fund aggregate calculated value (GRFACV) or reporting fund aggregate calculated value (RFACV) rather than gross asset value or NAV, if its NAV and gross asset value are not calculated monthly. RFACV and GRFACV may be calculated using the adviser's own methodologies or those of its service providers, if those methodologies are consistent with information reported internally.

Inflows & Outflows. Advisers will be required to disclose all new contributions from investors to the reporting fund, as well as all withdrawals, redemptions, or other distributions of any kind to investors. Quarterly filers would provide this information for each month of the reporting period. Currently, these entities file quarterly but only report changes in inflows or outflows on an annual basis.

Beneficial Ownership. Currently, advisers specify the approximate percentage of a fund's equity beneficially owned by different investor groups. The amendments mandate more granular information; U.S. person or non-U.S. person designation would be required for beneficial owners that are broker-dealers, insurance companies, nonprofits, pension plans, or banking or thrift institutions. An indicator would be required for beneficial owners that are internal or external private funds.

Country-level information on a fund's beneficial owners is not required.

Withdrawal or Redemption Rights. Form PF currently requires only large hedge fund advisers to report whether each qualifying hedge fund provides investors with withdrawal or redemption rights. The final rule requires all advisers to provide this information for each reporting fund. All advisers must indicate whether a reporting fund is an open-end private fund[3] or a closed-end private fund.[4] If a fund is neither, a detailed explanation must be provided. If the reporting fund is an open-end private fund, an adviser must indicate how often withdrawals or redemptions are permitted from the list of categories and what percentage of the fund's NAV may be—or is—subject to a suspension of—or material restrictions on—investor withdrawals/redemptions by an adviser. The adviser will be required to report this information regardless of whether there are notice requirements, gates, lockups, or other restrictions on withdrawals or redemptions.

Fund Performance. All advisers must provide gross and net fund performance (in the fund's base currency) reported to current and prospective investors and counterparties using a prescribed table. To promote consistency, an adviser must report its performance as a money-weighted internal rate of return[5] (IRR) (instead of a time-weighted return), if the reporting fund's performance used an IRR since inception. An adviser also must indicate whether the IRR reported includes the impact of subscription facilities. If a daily market value is calculated for any position in the reporting fund's portfolio, an adviser must report whether the reporting fund had one or more days with a negative daily rate of return during the reporting period. If so, advisers will be required to report (in the base currency):

- The most recent peak-to-trough drawdown, and indicate whether the drawdown was continuing on the data reporting date
- The largest peak-to-trough drawdown
- The largest single-day drawdown
- The number of days with a negative daily rate of return in the reporting period

All Hedge Funds (§1c)

Section 1c requires advisers to report information about the hedge funds they advise. More detailed reporting would be required about investment strategies, counterparty exposures, and trading and clearing mechanisms.

Investment Strategies. To promote consistency, advisers must indicate (from a drop-down list) which investment strategies best describe the reporting fund's strategies on the **last day of the reporting period**, rather than allowing advisers flexibility to report information as of the data reporting date or throughout the reporting period, as Form PF currently provides. New sub-categories under equity and credit strategies have been added and new categories have been added for real estate and digital assets.

Counterparty Exposures. Advisers to hedge funds (other than qualifying hedge funds) would have a new required table on a fund's exposures to creditors and counterparties and exposures creditors and counterparties have to a reporting fund. Advisers would report the U.S. dollar value of the reporting fund's borrowing and collateral received and its lending and posted collateral aggregated across all counterparties, including central clearing counterparties (CCPs) as of the end

[3] An open-end private fund is defined as a private fund that offers redemption rights to its investors in the ordinary course, which may be paid in cash or in kind, irrespective of redemption frequency or notice periods and without regard to any suspensions, gates, lockups, or side pockets that may be employed by the fund.
[4] A closed-end private fund is defined as any private fund that only issues securities, the terms of which do not provide a holder with any right, except in extraordinary circumstances, to withdraw, redeem, or require the repurchase of such securities, but which may entitle holders to receive distributions made to all holders pro rata.
[5] Internal rate of return is defined as the discount rate that causes the net present value of all cash flows throughout the life of the fund to be equal to zero.

of the reporting period. Advisers must identify each creditor or other counterparty (including CCPs) (up to five) to which the reporting fund owes (before posted collateral) an amount equal to or greater than either 5% of NAV as of the data reporting date or $1 billion. An adviser also must identify counterparties (up to five) for which the fund has net mark-to-market counterparty credit exposure, which is equal to or greater than either 5% of the reporting fund's NAV as of the data reporting date or $1 billion, net of collateral received or posted by the fund. Currently, the top five counterparties are disclosures regardless of the exposure size.

Trading & Clearing Mechanisms. Currently, disclosures about the extent of a fund's activities that are conducted on and away from regulated exchanges and clearing systems are reported as a **percentage** of value and trading volumes; actual **values** will now be required. Interest rate derivatives would be broken out separately from other derivatives and the following estimated amounts would be required:

- Traded on a regulated exchange or swap execution facility
- Traded over-the-counter (OTC) and cleared by a CCP
- Traded OTC or bilaterally transacted (and not cleared by a CCP)

Because sponsored repos have a different structure than other repos (the Fixed Income Clearing Corporation serves as the counterparty), the final rule requires these to be broken out separately from other repos. To reduce diversity in practice, the amendments also clarify that reverse repos must be reported with repos.

Large Hedge Fund Advisers (§2a & §2b)

A private fund adviser must complete §2 of Form PF if it had at least $1.5 billion in hedge fund AUM. A separate §2 must be filed for:

- Any qualifying hedge fund advised (a hedge fund with $500 million NAV)
- Each parallel fund that is part of a parallel fund structure that—in the aggregate—comprises a qualifying hedge fund (even if that parallel fund is not itself a qualifying hedge fund)
- The master fund of any master-feeder arrangement that—in the aggregate—comprises a qualifying hedge fund (even if that master fund is not itself a qualifying hedge fund)

In the first quarter of 2023, there were 2,034 qualifying hedge funds reported on Form PF—managed by 570 advisers—with almost $8 trillion in gross AUM, which represented almost 84% of the reported hedge fund assets.

New details are required on investment exposures, borrowing and counterparty exposure, market risk factors, risk metrics, and portfolio liquidity. Borrowing would be redefined to include synthetic long positions. The existing fair value hierarchy disclosures also would include the date the categorization was performed. Cash and equivalents would be reported separately, and government securities would be removed from the cash and cash equivalents definition. Digital assets would be excluded from cash and cash equivalents and broken out separately.

The amendments eliminate the current requirement to report certain aggregate data about the hedge funds managed as well as the following items:

- If the hedge funds have a single primary investment strategy or multiple strategies
- The percentage of the hedge fund's NAV that was managed using high-frequency trading strategies

Investment Exposure Reporting. The final rule makes the following changes:

- Replace the current table format with a drop-down menu.
- Require reporting based on instrument type within sub-asset classes to identify whether the fund's investment exposure is achieved through cash or physical investment exposure, through derivatives or other synthetic positions, or indirectly, *e.g.*, through a pooled investment such as an exchange-traded fund, an investment company, or a private fund. Disclosure is required for each month of the reporting period.
- Adjusted exposure reporting. For each sub-asset class, require (in addition to value as currently reported) the calculation of adjusted exposure that allows netting across instrument types for the same reference asset within each sub-asset class, and, for fixed income, within a prescribed set of maturity buckets.
- Uniform interest rate risk reporting. Sub-asset classes with interest rate risk must use the 10-year zero coupon bond equivalent. Advisers currently have an option to report either duration, weighted average tenor, or 10-year equivalents.
- Updated list of reportable sub-asset classes. Additional explanatory information will be required if the catch-all sub-asset class category equals or exceeds either 5% of the reporting fund's NAV or $1 billion. Changes to sub-asset classes:

  - Add sub-asset classes for listed equity securities—single name listed equities, indexes on listed equities, and American depository receipts
  - New sub-asset classes for repo and reverse repo positions, based on term
  - New sub-asset classes for asset-backed securities and other structured products
  - New and revised existing derivative sub-asset classes that capture certain derivatives, including certain credit and volatility and variance derivatives
  - Revisions to cash and cash equivalent sub-asset classes to break out U.S. and non-U.S. currency holdings and more granular commodities sub-asset classes
  - New sub-asset class for digital assets. The SEC declined to define this asset class but notes that if a particular asset could be classified as both a digital asset and another asset, the adviser should report the asset as the non-digital asset. For example, a money market fund that is traded on a blockchain should be reported as a money market fund, rather than as a digital asset.

Open and Large Positions. Advisers to qualifying hedge funds must report the top five long and short netted positions and the top 10 netted long and short positions.

Open & Large Position Reporting	
Current	**New**
A fund's total number of open positions determined on the basis of each position and not with reference to a particular issuer or counterparty	The total number of "reference assets" to which a fund holds long and short netted exposure
The percentage of a fund's NAV and sub-asset class for each open position that represents 5% or more of a fund's NAV	The percentage of NAV represented by the aggregate netted exposures of reference assets representing the **top five** long and short netted exposures

Open & Large Position Reporting	
Current	**New**
	The percentage of NAV represented by the aggregate netted exposures of reference assets representing the **top 10** netted long and short exposures

Advisers also must provide certain information on a fund's reference assets to which the fund has gross exposure (as of the end of each month of the reporting period) as follows:

- Debt Security. One percent of NAV and the fund's gross exposure to the reference asset exceeds 20% of the size of the overall debt security issuance
- Listed Equity Security. One percent of NAV and the reporting fund's gross exposure to the reference asset exceeds 20% of average daily trading volume measured over 90 days preceding the reporting date
- Five percent of the reporting fund's NAV or $1 billion

Details for each reference asset include:

- The dollar value of all long and the dollar value of all short positions (in U.S. dollars) with legal and contractual rights that provide exposure to the reference asset
- Netted exposure to the reference asset
- Sub-asset class and instrument type
- Title or description of the reference asset
- Reference asset issuer (if any) name and LEI
- CUSIP (if any)
- If the reference asset is a debt security, the size of issue, and if the reference asset is a listed equity, the average daily trading volume, measured over 90 days preceding the reporting date

Counterparty Exposure. Similar to the hedge fund requirement above, qualifying hedge funds also will have a new consolidated counterparty exposure table. The fund must report, as of the end of each month of the reporting period, borrowings and other transactions with creditors and other counterparties for each of six categories:

- Unsecured
- Secured borrowing and lending under a prime brokerage agreement
- Secured borrowing and lending via repo or reverse repo
- Other secured borrowing and lending
- Derivatives cleared by a CCP
- Derivative positions not cleared by a CCP

For each of these six categories, a fund must include:

- Creditor type – U.S. depository institution, U.S. creditors that are not depository institutions, and non-U.S. creditors
- Collateral posted by type – Cash and cash equivalents, government securities, securities other than cash and cash equivalents and government securities and other types of collateral or credit support (including the face amount of

letters of credit and similar third-party credit support) received and posted by a reporting fund, and secured borrowing and lending (prime brokerage or other brokerage agreement)
- Report—at the end of each month of the reporting period—the expected increase in collateral required to be posted by the reporting fund if the margin increases by 1% of position size for each type of borrowing or other transaction

Borrowing. Advisers must identify all creditors and counterparties (including CCPs) where the amount a fund has **borrowed** (including any synthetic long positions) **before posted collateral** equals or is greater than either 5% of the fund's NAV or $1 billion. An adviser also must disclose all counterparties (including CCPs) where the **net mark-to-market counterparty credit exposure** is greater than either 5% of the fund's NAV or $1 billion.

Market Factor Effects. Advisers to qualifying hedge funds will be required to report all market factors to which their portfolio is directly exposed. Currently, advisers may omit a response to any market factor that they do not regularly consider in formal testing for a reporting fund's risk management. However, only one threshold will be required for each factor (rather than the current two). A new market test will be required to measure a change in a fund's exposure for a change in the slope of the yield curve.

Risk Metrics. The final rule will eliminate the requirement that an adviser indicate whether there are risk metrics other than—or in addition to—Value at Risk (VaR) that the adviser considers important to managing a reporting fund's risks.

Currency Exposure Reporting. A fund must report for each month of the reporting period (in U.S. dollars):

- The net long value and short value of a fund's currency exposure arising from foreign exchange derivatives and all other assets and liabilities denominated in currencies other than a fund's base currency
- Each currency to which the fund has long dollar value or short dollar value exposure equal to or exceeding either 5% of a fund's NAV or $1 billion

Financing and Investor Liquidity. Advisers will be required to provide the dollar amount of financing that is available to the reporting fund, including financing that is available but not used, by the following types:

- Unsecured borrowing
- Secured borrowing via prime brokerage
- Secured borrowing via reverse repo
- Other secured borrowings

Conclusion

The asset management team at **FORVIS** has more than 50 years of experience providing accounting, tax, and consulting services to various types of investment holdings, including conventional debt and equity investments, loans, businesses, alternative investments, and other unique assets. As of June 2023, Convergence Optimal Performance ranked FORVIS as a top 20 accounting and audit firm to registered investment advisers. FORVIS also was ranked in the top 20 by AUM. We have experience providing services to funds ranging from emerging managers to $100-plus billion in AUM. Our knowledge allows us to provide tailored services to help meet your unique needs. We provide services to private, public, and Cayman funds. For more information, visit forvis.com.

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Appendix

Form PF	Smaller private fund advisers	Large hedge fund advisers	Large liquidity fund advisers	Large private equity fund advisers
Section 1a and section 1b (basic information about the adviser and the private funds it advises) **The final rules modify section 1a and section 1b**	Annually	Quarterly	Quarterly	Annually
Section 1c (additional information concerning hedge funds) **The final rules modify section 1c**	Annually, if they advise hedge funds	Quarterly	Quarterly, if they advise hedge funds	Annually, if they advise hedge funds
Section 2 (additional information concerning qualifying hedge funds) **The final rules modify section 2**	No	Quarterly	No	No
Section 3 (additional information concerning liquidity funds) **No final revisions**	No	No	Quarterly	No
Section 4 (additional information concerning private equity funds) **No final revisions**	No	No	No	Annually
Section 5 (current reporting concerning qualifying hedge funds)[1] **No final revisions**	No	As soon as practicable upon a current reporting event, but no later than 72 hours	No	No
Section 6 (event reporting for private equity fund advisers)[1] **No final revisions**	Within 60 days of fiscal quarter end upon a reporting event, if they advise private equity funds	No	No	Within 60 days of fiscal quarter end upon a reporting event
Section 7 (temporary hardship request)[1] **The final rules revise the filing instructions**	Optional, if they qualify	Optional, if they qualify	Optional, if they qualify	Optional, if they qualify
Transition Filings (indicating the adviser is no longer obligated to file on a quarterly basis) **No final revisions**	Not applicable	If they cease to qualify as a large hedge fund adviser	If they cease to qualify as a large liquidity fund adviser	Not applicable
Final Filings (indicating the adviser is no longer subject to the rules) **No final revisions**	If they qualify	If they qualify	If they qualify	If they qualify

Source: SEC

1) The SEC previously adopted amendments to Form PF in May 2023, which added sections 5 and 6 and redesignated the previous section 5 as section 7 (see "SEC Finalizes First Round of Form PF Updates").