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Connecticut Department of Banking Releases Orders Clarifying Investment Adviser Registration and Regulation

On July 11, 2011, the State of Connecticut Department of Banking (the "Department") released three Orders regarding Connecticut investment adviser registration and regulation.[1] Among other things, the Orders provide that investment advisers currently exempt from registration with the Department because they are relying on the federal "private adviser exemption"<sup[2]< sup> under the Investment Advisers Act of 1940, as amended (the "Advisers Act"), and that will no longer be eligible for registration with the Securities and Exchange Commission ("SEC") or qualify for an exemption from registration, shall have until March 30, 2012, to register as an investment adviser with the Department. As discussed in the Day Pitney Alert dated July 11, 2011, the SEC recently issued its final rules and rule amendments[3] implementing Title IV of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"), which, among other things, (1) rescinded the private adviser exemption effective July 21, 2011; (2) generally increased the statutory threshold for SEC registration for investment advisers from $25 million in assets under management ("AUM") to $100 million AUM for most U.S. advisers; and (3) extended the deadline for investment adviser registration for advisers previously relying on the private adviser exemption to March 30, 2012. The Department's Orders seek to clarify the registration requirements for investment advisers with certain ties to Connecticut, which requirements became unclear in the wake of Dodd-Frank and the SEC's related rules. Absent the Department's Orders, as a result of Dodd-Frank's repeal of the private adviser exemption and the addition of new exemptive provisions to Section 203 of the Advisers Act, investment advisers that (i) have a place of business within Connecticut or (ii) during the preceding 12 months had more than five clients who are residents of Connecticut, and previously relied on such exemptions would generally be required to register immediately as investment advisers under the Connecticut Uniform Securities Act ("CUSA"). The Orders create a registration transition period for previously exempt advisers and provide several new exemptions from registration with the Department. The first Order ("Transition Order") establishes a state registration timetable for investment advisers affected by Dodd-Frank. The second Order ("Exemptions Order") governs certain investment advisers exempt from registration following passage of Dodd-Frank. The third Order ("Client Counting Order") amends and restates a March 4, 1999, Department Order defining the term "client" for purposes of the Connecticut de minimis exemption for investment advisers. **The Transition Order** The Transition Order creates a definitive timetable for investment advisers that, as a result of Dodd-Frank, need to now register or make notice filings with the Department. Section 36b-6(c)(1) of CUSA provides, in part: "No person shall transact business in this state as an investment adviser unless registered as such by the commissioner...or exempted pursuant to subsection (e) of this section." Subsection (e) of Section 36b-6 of CUSA exempts from state registration any investment adviser that is registered or required to be registered under Section 203 of the Advisers Act, and requires that such investment adviser first file with the Commissioner of the Department (the "Commissioner") a notice of exemption and pay a nonrefundable filing fee. On October 14, 1997, the Commissioner issued an Order Governing Certain Federally Exempt Investment Advisers ("1997 Order"), which excluded from the Connecticut definition of "investment adviser" those firms that, but for Section 203(b)(3) of the Advisers Act (the private adviser exemption), as then constituted, would have been required to register with the SEC. Dodd-Frank's repeal of the private adviser exemption, effective July 21, 2011, effectively nullifies the 1997 Order and exemption for those investment advisers that have a place of business within Connecticut or during the preceding 12 months had more than five clients who are residents of Connecticut (i.e., those that would have met the Connecticut definition of "investment adviser" but for the private adviser exemption). Accordingly, the Transition Order provides that in light of the legal and operational complexities surrounding implementation of Dodd-Frank, the following classes of investment advisers shall have until the dates specified below to fulfill applicable state registration or notice filing requirements under CUSA, absent an exclusion or exemption:

- Investment advisers relying on the private adviser exemption on July 20, 2011, that, due to their AUM and the unavailability of another exemption under the Advisers Act, shall have until March 30, 2012, to register as investment advisers with the Department.
- Investment advisers registered with the SEC after July 11, 2011, that have AUM less than $90 million as of March 30, 2012, shall have until the earlier of the effective date of their withdrawal from registration with the SEC or June 28, 2012, to register as investment advisers with the Department.
- Investment advisers relying on the transition period in Advisers Act Rule 203-1(e), that otherwise would have to register as investment advisers with the SEC and file a notice with the Department due to the repeal of the private adviser exemption, may defer the filing of a notice under Section 36b-6(e) of CUSA until March 30, 2012. Such advisers shall not be required to register as investment advisers under CUSA during the deferment of federal registration until March 30, 2012.

Furthermore, the Transition Order provides that effective July 21, 2011, having been superseded by Dodd-Frank's repeal of Section 203(b)(3) of the Advisers Act, the 1997 Order is rescinded and shall no longer be in force and effect. **The Exemptions Order** In addition to repealing the private adviser exemption, Dodd-Frank also amended Section 203 of the Advisers Act to (1) add an exemption in Section 203(b)(3) for "foreign private advisers" (2) modify the exemption in Section 203(b)(6) to cover certain commodity trading advisors advising a private fund; (3) add an exemption in Section 203(b)(6) for investment advisers to small business investment companies ("SBICs"); (4) add an exemption in Section 203(l) for advisers to venture capital funds; and (5) add an exemption in Section 203(m) for investment advisers that solely advise private funds having less than $150 million in AUM in the United States. Recently, as noted above, the SEC promulgated final rules and rule amendments under Section 203 of the Advisers Act affecting, among others, those advisers described above. Section 36b-31(c) of CUSA provides: "To encourage uniform interpretation and administration of [the regulation of investment advisers], the commissioner may cooperate with...the Securities and Exchange Commission." Further, under Section 36b-1(a) of CUSA, "[t]he commissioner may from time to time make, amend and rescind such...orders as are necessary to carry out the provisions of Section 36b-2 to 36b-34."[4] Accordingly, the Exemptions Order provides that the following investment advisers shall be exempt from the registration requirements under Section 36b-6(c)(1) of CUSA:

- Investment advisers that are "foreign private advisers" under Sections 202(a)(30) and 203(b)(3) of the Advisers Act.
- Investment advisers that are registered with the Commodity Futures Trading Commission as trading advisors and fulfill the conditions for exempt treatment under Section 203(b)(6) of the Advisers Act.
- Investment advisers that qualify for the SBIC exemption in Section 203(b)(7) of the Advisers Act.
- Investment advisers that qualify under Section 203(l) of the Advisers Act as advisers solely to one or more "venture capital funds" as defined in Advisers Act Rule 203(l)-1. Investment advisers relying on this exemption must make certain reports in electronic format to the Investment Adviser Registration Depository ("IARD"), as required by Advisers Act Rule 204-4. This exemption incorporates by reference the provision in Advisers Act Rule 203(l), which grandfathers as a "venture capital fund" certain preexisting funds that, among other things, do not sell securities in their funds to any person after July 21, 2011.[5]
- Investment advisers that qualify under Advisers Act Section 203(m) as advisers solely to private funds, as defined in Section 202(a)(29) of the Advisers Act, and that have AUM in the United States of less than $150 million. Investment advisers relying on this exemption must make certain reports in electronic format to the IARD, as required by Advisers Act Rule 204-4.

Additionally, any individual employed by or associated with an investment adviser relying on the preceding exemptions shall be exempt from having to register as an investment adviser agent under Section 36b-6(c)(2) of CUSA. **The Client Counting Order** The Client Counting Order provides that, for purposes of Section 36b-6(e)(3) of CUSA, the term "client" shall be determined in accordance with Advisers Act Rule 202(a)(30)-1, without regard to paragraph (b)(4) of that section. Under Rule 202(a)(30)-1, an adviser may treat the following as a single client:

- A natural person and that person's minor children; any relative, spouse, or relative of the spouse of that person who has the same principal residence of such person; and all accounts of which that person and/or the person's minor child or relative, spouse, or relative of the spouse who has the same principal residence of