By Overlooking Form PF, Hedge Managers Invite Risk

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At a recent thought leadership dinner with chief financial and operating officers of several well-known hedge funds, I asked the question, "Who here is preparing for Form PF?" You might be surprised to know that the majority response was, "What's Form PF?"

With so many changes happening at such a rapid pace, this important outcome of the Dodd-Frank Act had gone largely unnoticed. Those who were aware are sitting tight to see whether Form PF would materialize in its proposed form.

To summarize, the SEC issued a draft version of Form PF in February of this year; requesting industry comments until April. At the time, the “form” was a 44-page filing document that all registered advisors to private funds would need tocomplete, at least in part. The proposed deadline for the first filing was January 15th, 2012 and the task would have, in short, been onerous.

Fortunately for the industry, the requirements and thresholds have changed and the timeframes have been extended. The minimum reporting requirement is $150 million AUM. Large private advisors are now defined as having at least $1.5billion AUM attributable to hedge funds, which is changed from the proposed $1 billion across all funds and accounts.

Large private advisors now have 60 days in which to file. The SEC increased this from the proposed 15 days citing, “We want the information that will be reported to regulators on Form PF to be useful. It will not be useful if it is rushed or incomplete”.

Smaller advisors now have 120 days to file only Section 1) vs. the originally proposed 90 days. Initial filing periods have been extended for most private fund advisors following the end of their first fiscal year or calendar quarter, as applicable, to end on or after December 15th, 2012.

Advisors with at least $5 billion AUM attributable to hedge funds will be required to file following the end of their first fiscal year or calendar quarter, as applicable, to end on or after June 15th, 2012.

CFOs, COOs, CCOs are breathing a sigh of relief.

Changes to the data requirements have yet to be confirmed, we will have to wait until after the Commodity Futures Trading Commission votes on the form. However, it is clear that fund managers now will have more time to assess how to deal with Form PF. This reprieve may be short lived. Form PF will still likely be a time-consuming exercise and few funds are equipped to aggregate the significant levels of data required. Geographical, credit, counterpart, sector and strategy exposure is only part of the story.

Today, few managers or service providers are in a position to deliver the data required for Form PF, specifically normalized to the SEC's view of the world. For example, funds choosing to implement portfolio accounting or data warehousing will have to start those ventures by Q2 2012 at the latest. Managers above $5bn AUM who have to file after June 15th must already have technology in place.

Ignoring Form PF beyond the end of 2011 could introduce very real business risk.

In other words, managers will need to allow ample time to fully assess the form, their data sources and to explore technology options. Managers must enter 2012 by drafting a plan to identify each data component determining where the data is coming from and in what format. Then comes the task of getting definitive answers as to whether the anticipated data sources can be delivered in the right format and in the appropriate timeframe.

Managers also need to understand that Form PF needs to be approved by all business stakeholders; it's not just the responsibility of the CCO or CFO. Creating a task force will engage the entire organization ensuring the process of filing moves towards an automated environment, where best practices optimize this crucial business deliverable. Daily reconciliation, understanding the changes in data and addressing breaks and discrepancies in the date will become the ideal state.

Execution is critical. Investors may very well use Form PF as a benchmark in initial and ongoing due diligence, not just to gain additional transparency, but to determine the strength of your operations and accounting groups and to judge the strength of your business.

Today, the number of tangible, practical solutions from the service provider community is small. With clarity and the benefit of time, one would hope that service providers as a whole will make good use of this to ease the burden on their clients. If that doesn't happen and industry procrastination continues, it is quite possible that there will be an excess of clients looking for assistance in an environment where there won't be enough providers who can help. Nobody wants to be stuck without a chair when the music stops.

For more information on Form PF checkout: http://www.sec.gov/news/press/2011/2011-226.htm

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