INVESTMENT MANAGEMENT ALERT

JUNE 2001

CONSUMER PRIVACY RULES: COMPLIANCE BY PRIVATE INVESTMENT FUND MANAGERS

If you are the general partner or manager of a hedge fund, a private equity fund or any other private investment fund that has any individual investors, you are subject to new federal rules designed to protect the privacy of information you obtain concerning those individuals. These new federal rules (the Privacy Rules) require you to (1) adopt policies and procedures to safeguard certain personal information about prospective and existing investors and (2) give initial and annual notices to prospective and existing investors about these policies and procedures. The Privacy Rules apply to you even if you are not registered with the Securities and Exchange Commission (SEC) or any other financial services industry regulator.

For most private investment fund managers, the deadline for compliance with the new Privacy Rules is July 1, 2001. By that date, you are required to have delivered an initial privacy notice to all existing individual investors in the funds that you manage. (If you are registered with the Commodity Futures Trading Commission (CFTC) and are not registered with the SEC, you may have additional time to comply with respect to investors in commodity pools that you manage.)

Immediate Compliance Action Required

In order to comply with the Privacy Rules, the following actions need to be taken as soon as possible by private investment fund managers:

- adopt privacy policies and implement procedures to safeguard the collection and disclosure of all "consumer" or "customer" information that constitutes "nonpublic personal information" (Protected Information)
- determine whether you need to comply with the "opt-out" requirements of the Privacy Rules because you plan to share Protected Information with nonaffiliated third parties
- review your agreements and other contractual arrangements with nonaffiliated third parties to determine whether disclosure sharing is permitted. Amend these agreements in accordance with the requirements of the Privacy Rules
- by July 1, 2001, deliver your initial phase-in notices to all existing clients/investors and, if applicable, to prospective clients/investors (with an opt-out).

We can assist you in complying with the requirements of the Privacy Rules as they apply to you.

Which Rules Apply

Private investment fund managers of funds having any individual investors are subject to at least one of the following three sets of Privacy Rules:

- if you are registered with the SEC, you are subject to the SEC's Privacy Rules

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- if you are registered with the CFTC, you are subject to the CFTC's Privacy Rules
- if you are not registered with the SEC or the CFTC (and you are not regulated by any other financial services industry regulator), you are subject to the Privacy Rules of the Federal Trade Commission (FTC).

This memorandum provides a brief summary of the relevant provisions of the Privacy Rules as they apply to managers of private investment funds. This memorandum is not intended to be an exhaustive treatment of the Privacy Rules, but is supplied to help you understand the basic regulatory requirements as they relate to private investment funds, so that you can take the necessary actions to meet the compliance deadline.

This memorandum is not intended for banks or other financial institutions that are subject to regulation under banking laws.

Privacy Rules Apply to "Financial Institutions," Including Private Investment Funds

The Privacy Rules apply to all "financial institutions." This term is broadly defined to include (among others) SEC-registered investment advisers and investment companies, as well as CFTC-registered commodity pool operators and commodity trading advisors. The FTC has concluded that hedge funds and other private investment funds are "financial institutions." That is why general partners or managers of such funds, even if they are not registered with the SEC, the CFTC or another regulator, must comply with the Privacy Rules.

Privacy Rules Protect Individuals, Not Businesses

The Privacy Rules are intended to protect *individuals* rather than business entities. An "individual" is any natural person, or his/her legal representative and any holder of an individual retirement account. The Privacy Rules extend to U.S. and foreign individuals. (However, we have been advised by the FTC that its Privacy Rules are not necessarily intended to cover offshore funds marketed primarily to non-U.S. investors.)

"Consumers" and "Customers"

The Privacy Rules provide protections for both "consumers" and "customers."

"Consumers." If you collect Protected Information from prospective investors who have not yet established a contractual relationship with you (or a fund that you manage), these applicants are deemed to be "consumers." While consumers are protected under the Privacy Rules, you need only provide a notice to a consumer if you intend to share the consumer's Protected Information with certain nonaffiliated third parties.

A consumer relationship is established at the point when an individual (U.S. or foreign) provides Protected Information to you when seeking to obtain either investment advisory or other financial services from you, whether or not you ultimately approve or deny the application. For example, if you are a fund manager, a "consumer" relationship with a prospective investor is established at the point the investor submits a completed subscription questionnaire for your review.

"Customers." Once you provide or agree to provide a financial product or service to an individual, the status of the consumer is changed to a "customer." This is significant because, under the Privacy Rules, you must provide an initial phase-in notice by July 1, 2001, and an annual notice thereafter to *all* customers. All new customers after the July 1 date must receive an initial notice at the time the customer relationship is established. In the case of a private investment fund, a customer relationship is established at the time the subscription agreement is accepted by the fund (or the general partner). Placing your privacy notice and sharing practices in the subscription document in a clear and conspicuous manner would satisfy the initial notice delivery requirements.

If you do not reserve the right to share Protected Information with any nonaffiliated third party, except as permitted under the Privacy Rules, you may provide a short-form or simplified notice to your customers. On the other hand, if you do reserve this right, then a standard notice containing greater detail as to your business practices and an opt-out provision must be provided. The contents of the notice and the manner of delivery are discussed in greater detail below.

Required Notices to Consumers and Customers

All notices must identify your privacy policies and sharing practices in a "clear and conspicuous" manner. "Clear and conspicuous" means that a notice is reasonably understandable and designed to call attention to the nature and significance of information in the notice.

Information Included in Privacy Notices. Any standard initial, annual or revised privacy notice must contain, at a minimum, the following information:

(i) the categories of Protected Information that you collect

(ii) the categories of Protected Information that you disclose

(iii) the categories of affiliates and nonaffiliated third parties to whom you disclose Protected Information, other than certain permitted parties

(iv) the categories of Protected Information about your former customers that you disclose and the categories of affiliates and nonaffiliated third parties to whom you disclose such Protected Information, other than to certain permitted parties

(v) if you disclose Protected Information to a nonaffiliated third party for which no exception applies, a separate statement of the categories of Protected Information you disclose and the categories of third parties with whom you have contracted

(vi) if you disclose Protected Information as described in (v) above, you must provide a right to opt-out of such disclosure and provide the method to exercise that right (via toll free telephone number, return envelope or any other reasonable method)

(vii) any disclosures that you make under the Fair Credit Reporting Act

(viii) your policies and practices with respect to protecting the confidentiality and security of Protected Information. To satisfy this provision you must (a) describe in general terms who is authorized to have access to the information, and (b) state whether you have security practices and procedures in place to ensure the confidentiality of the information in accordance with your policy. You do not have to describe the technical information about the safeguards you use

(ix) any other disclosure as to nonaffiliated third parties that are subject to exceptions under the Privacy Rules.

Short-Form Notice (no Opt-out). If you do not disclose, and do not wish to reserve the right to disclose, Protected Information about customers or former customers to nonaffiliated third parties, except as permitted under certain exceptions to the Privacy Rules, you may provide a simplified notice and state that you do not disclose any Protected Information about your customers or former customers to anyone, except as permitted by law, together with descriptions required under sections (i), (viii) and (ix) above.

Annual Notice. Over the course of a continuing customer relationship with your clients/investors, you are required to deliver to all clients/investors annual privacy notices. You are permitted to select a calendar year or a 12-month period within which you provide this annual notice. The first annual notice must be delivered at any point in the calendar year following the year in which the customer

relationship was established. This policy must be applied to customers on a consistent basis.

Opt-out Provision

If you are required to provide a disclosure opt-out to any of your prospective or existing clients/investors, you must:

- state that the prospective or existing client/investor has the right to opt-out of that disclosure
- state that you disclose or reserve the right to disclose Protected Information about the prospective or existing client/investor to a nonaffiliated third party
- provide a reasonable means by which this opt-out right may be exercised.

An opt-out election must be honored as soon as reasonably practicable, and that election survives until revoked by the prospective or existing client/investor.

Written and Electronic Notice

You must provide any privacy and opt-out notices so that each client/investor can reasonably be expected to receive actual notice of the policy, which may be in writing, or, if the client/investor agrees, electronically. Therefore, you may provide notice of your privacy and opt-out policies on your Web site, but only if (1) your client/investor has agreed to receive notices at the Web site, and (2) you continuously post a current notice of your privacy policies and practices in a clear and conspicuous manner on the site. You should place the notice, or a link to the notice, on a screen that your clients/investors frequently access. If your client/investor agrees to electronic delivery of information, you may provide your opt-out notice on a form that can be sent out via e-mail or set up a process on the web site in which the client/investor is able to make the opt-out election.

Permitted Disclosures

The Privacy Rules contain various exceptions permitting disclosures that are not subject to the opt-out provision. For example, you may be permitted to share information with a nonaffiliated third party without providing your prospective or existing clients/investors a right to opt-out if the third party is to perform certain services for you (*i.e.*, to a clearing agent if you are a registered broker-dealer). Third parties falling under these exceptions include your attorneys, accountants and auditors. To qualify for the exception, you must first enter into a contractual agreement with the third party, and the agreement must prohibit the third party from disclosing or using the information other than to carry out the purposes for which you disclose the information. If you entered into such a contract on or before July 1, 2000, you have until July 1, 2002, to amend the contract to comply with this requirement.

The SEC and FTC have each stated that if you hired the agent to carry out certain responsibilities for your customers, you are responsible for the handling of Protected Information your agent has access to. Those third parties that provide such services will be subject to a limitation on the reuse of Protected Information accessible to them in the course of their duties. Accordingly, a nonaffiliated third party that receives Protected Information must not disclose the information to any other person that is not affiliated with either you or the third party, unless the disclosure would be lawful if made directly by you, such as by virtue of an exception to disclosure or if the disclosure was made by you in compliance with a notice you provided to the customer.

IF YOU HAVE ANY QUESTIONS CONCERNING THE PRIVACY RULES, PLEASE CONTACT:

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