List of Subjects in 14 CFR Part 107

Aircraft, airmen, Aviation safety, Reporting and recordkeeping requirements.

Accordingly, the FAA corrects 14 CFR part 107 by making the following technical amendments:

PART 107—SMALL UNMANNED AIRCRAFT SYSTEMS

■ 1. The authority citation for part 107 continues to read as follows:

Authority: 49 U.S.C. 106(f), 40101 note, 40103(b), 44701(a)(5), 46105(c), 46110, 44807.

§ 107.110 [Amended]

■ 2. Amend § 107.110 by redesignating paragraphs (b) and (c) and paragraphs (a)(2) and (b), respectively.

■ 3. Amend § 107.125 by revising paragraph (a)(2) to read as follows:

§ 107.125 Category 3 operations: Operating requirements.

* * * * *

(a) * * *

(2) Is listed on an FAA-accepted declaration of compliance as eligible for Category 3 operations in accordance with § 107.160; and

* * * * *

Issued in Washington, DC, under the authority provided by 49 U.S.C. 106(f), 40101 note and 44807.

Caitlin Locke,

Acting Deputy Executive Director, Office of Rulemaking, Federal Aviation Administration.

[FR Doc. 2021–24550 Filed 11–9–21; 8:45 am]

BILLING CODE 4910–13–P

SECURITIES AND EXCHANGE COMMISSION

17 CFR Part 275

[Release No. IA–5904]

Performance-Based Investment Advisory Fees

AGENCY: Securities and Exchange Commission.

ACTION: Final rule.

SUMMARY: The Securities and Exchange Commission (''Commission'' or ''SEC'') is adopting amendments to the rule under the Investment Advisers Act of 1940 (''Advisers Act'') that permits investment advisers to charge performance-based compensation to ''qualified clients.'' The rule defines ''qualified client'' with reference to specific dollar amount thresholds, which are required to be adjusted every five years to account for the effects of inflation. These amendments replace specific dollar amount thresholds in the rule's ''qualified client'' definition with references to the Commission's ''most recent order,'' as defined by the amended rule, containing the specific dollar amount thresholds adjusted for inflation.

DATES: The amendments are effective on November 10, 2021.

FOR FURTHER INFORMATION CONTACT: Matthew Cook, Senior Counsel, at (202) 551–6787 or *IArules@sec.gov,* Investment Adviser Regulation Office, Division of Investment Management, Securities and Exchange Commission, 100 F Street NE, Washington, DC 20549–8549.

SUPPLEMENTARY INFORMATION: The Commission is adopting amendments to 17 CFR 275.205–3 (rule 205–3) under the Advisers Act.[1]

I. Background

Section 205(a)(1) of the Advisers Act generally prohibits an investment adviser registered or required to be registered with the Commission from entering into, extending, renewing, or performing any investment advisory contract that provides for compensation to the adviser based on a share of capital gains on, or capital appreciation of, the funds of a client.[2] Congress restricted these compensation arrangements (also known as performance compensation or performance fees) in 1940 to protect advisory clients from fee arrangements it believed could encourage advisers to engage in speculative trading practices while managing client funds in order to realize or increase advisory fees.[3] Congress subsequently authorized the Commission to exempt any advisory contract from the performance fee prohibition if the contract is with any person that the Commission determines does not need the protections of this restriction.[4] Rule 205–3 under the Advisers Act exempts an investment adviser from the prohibition against charging a client performance fees when the client is a ''qualified client.''[5] A qualified client includes a client that has at least a certain dollar amount in assets under management with the adviser immediately after entering into the advisory contract (''assets-under-management test''), and a client that the adviser reasonably believes, immediately prior to entering into the contract, had a net worth of more than a certain dollar amount (''net worth test'').[6]

The Dodd-Frank Wall Street Reform and Consumer Protection Act (''Dodd-Frank Act'')[7] amended section 205(e) of the Advisers Act to provide that, by July 21, 2011, and every five years thereafter, the Commission shall, by order, adjust for the effects of inflation the dollar amount thresholds included in rules issued under section 205(e), rounded to the nearest multiple of $100,000.[8] In 2011, the Commission issued an order to revise the dollar amount thresholds of the assets-under-management and net worth tests to $1,000,000 and $2,000,000, respectively.[9] In 2012, the Commission amended rule 205–3 to codify the dollar amount thresholds in the 2011 Order and, among other

[1] 15 U.S.C. 80b. Unless otherwise noted, all references to statutory sections are to 15 U.S.C. 80b of the United States Code, at which the Advisers Act is codified, and all references to rules under the Advisers Act, including rule 205–3, are to title 17, part 275 of the Code of Federal Regulations [17 CFR part 275].

[2] 15 U.S.C. 80b–5(a)(1).

[3] *See* Exemption to Allow Registered Investment Advisers to Charge Fees Based Upon a Share of Capital Gains Upon or Capital Appreciation of a Client's Account, Investment Advisers Act Release No. 996 (Nov. 14, 1985) [50 FR 48556 (Nov. 26, 1985)] (''1985 Adopting Release''), at Section I.A and footnote 3.

[4] Section 205(e) of the Advisers Act. Section 205(e) provides that the Commission may determine that persons do not need the protections of section 205(a)(1) on the basis of such factors as ''financial sophistication, net worth, knowledge of and experience in financial matters, amount of assets under management, relationship with a registered investment adviser, and such other factors as the Commission determines are consistent with [section 205].''

[5] 1985 Adopting Release, *supra* footnote 3. The exemption applies to the entrance into, performance, renewal, and extension of advisory contracts. *See* rule 205–3(a).

[6] Rule 205–3(d)(1)(i) through (ii). The dollar amount thresholds of the assets-under-management and net worth tests were $500,000 and $1 million, respectively, when the Commission adopted rule 205–3 in 1985. *See* 1985 Adopting Release, *supra* footnote 3. In 1998, the Commission amended rule 205–3 to, among other things, revise the dollar amounts of the assets-under-management test and net worth test to adjust for the effects of inflation since 1985 (the amounts were adjusted to $750,000 and $1.5 million, respectively). *See* Exemption To Allow Investment Advisers To Charge Fees Based Upon a Share of Capital Gains Upon or Capital Appreciation of a Client's Account, Investment Advisers Act Release No. 1731 (July 15, 1998) [63 FR 39022 (July 21, 1998)]. These dollar amount thresholds were subsequently adjusted to account for the effects of inflation by Commission orders in 2011, 2016 and 2021, as discussed *infra* footnotes 9, 11, and 12 and accompanying text.

[7] Public Law 111–203, 124 Stat. 1376 (2010).

[8] *See* section 418 of the Dodd-Frank Act (requiring the Commission to issue an order every five years revising dollar amount thresholds in a rule that exempts a person or transaction from section 205(a)(1) of the Advisers Act if the dollar amount threshold was a factor in the Commission's determination that the person does not need the protections of that section).

[9] Order Approving Adjustment for Inflation of the Dollar Amount Tests in Rule 205–3 under the Investment Advisers Act of 1940, Investment Advisers Act Release No. 3236 (July 12, 2011) [76 FR 41838 (July 15, 2011)] (''2011 Order'').

amendments, to add a new paragraph (e) that states that the Commission will issue an order on or about May 1, 2016, and approximately every five years thereafter, adjusting for inflation the dollar amount thresholds of the assets-under-management and net worth tests of the rule.[10]

Since then, the Commission has twice issued orders adjusting for the effects of inflation the dollar amount thresholds in accordance with rule 205–3(e). In 2016, the Commission issued an order increasing the dollar amount threshold of the net worth test (to $2,100,000) and maintaining the dollar amount threshold of the assets-under management test (at $1,000,000).[11] On June 17, 2021, the Commission issued an order, effective as of August 16, 2021, increasing the dollar amount threshold of the assets-under-management test from $1,000,000 to $1,100,000 and the dollar amount threshold of the net worth test from $2,100,000 to $2,200,000.[12]

II. Discussion

A. Amendments to Rule 205–3

We are adopting amendments to rule 205–3 to replace the specific dollar amount thresholds in the rule's net worth and assets-under-management tests with references to the ''most recent order'' issued by the Commission containing the specific dollar amount thresholds adjusted for inflation. We define ''most recent order'' in the rule to mean ''the most recently issued Commission order in accordance with paragraph (e) of this section and as published in the **Federal Register**.'' [13]

As discussed above, the Commission is required to issue an order every five years adjusting for inflation the dollar amount thresholds of the assets-under-management and net worth tests of the rule. By amending the rule to refer to the ''most recent order'' for the dollar amount thresholds in the rule's ''qualified client'' tests, the rule will reference the most recently issued and published adjusted dollar amounts,[14] and more directly tie the relevant amount to the mechanism by which it is established (*i.e.,* the order).

We are also adopting an amendment to rule 205–3 to update from ''May 1, 2016'' to ''May 1, 2026'' the reference point of a specific date in paragraph (e). Paragraph (e) currently provides that the dollar amount thresholds of the assets-under-management and net worth tests will be adjusted for inflation by Commission order ''issued on or about May 1, 2016 and approximately every five years thereafter.'' [15] By amending the rule to refer to a date in the future, the rule will establish clearly the next expected date for issuance of a Commission order, while retaining the five-year period between such orders that was established by the Commission in 2012. We believe that referring in the rule text to a specific date will be useful to market participants in determining approximately when the Commission will issue and the **Federal Register** will publish an order for purposes of the amended rule's definition of ''most recent order.''

B. Procedural and Other Matters

Under the Administrative Procedure Act (''APA''), notice of proposed rulemaking is not required: (1) For interpretive rules, general statements of policy, or rules of agency organization, procedure, or practice; or (2) when the agency for good cause finds (and incorporates the finding and a brief statement of reasons therefor in the rules issued) that notice and public procedure thereon are impracticable, unnecessary, or contrary to the public interest.[16] Given that the amendments to rule 205–3 do not substantively change the methodology for calculating the dollar amount thresholds or the amount of those thresholds, and instead merely add a reference in the rule to the Commission's ''most recent order'' adjusting the dollar amount thresholds and update the reference point of a specific date in paragraph (e), the Commission finds that good cause exists to dispense with public notice and comment pursuant to the notice and comment provisions of the APA. In accordance with the APA, the Commission also finds that there is good cause to establish an effective date less than 30 days after publication of rule 205–3.[17] The Commission finds there is good cause for the amendments to rule 205–3 to take effect upon publication in the **Federal Register** because the current rule's dollar thresholds do not conform to the dollar thresholds adopted pursuant to the most recent order. The Commission believes that establishing an effective date less than 30 days after publication of rule 205–3 is necessary to remove the outdated dollar thresholds in the rule by making the text consistent with the thresholds adopted pursuant to the most recent order. Furthermore, the amendments to rule 205–3 under the Advisers Act do not contain any ''collection of information'' requirements as defined by the Paperwork Reduction Act of 1995, as amended (''PRA'').[18] Accordingly, the PRA is not applicable.

III. Economic Analysis

The Commission is sensitive to the economic effects that could result from the amendments to rule 205–3. Investment advisers who charge, or may charge, performance fees and clients who meet, or may meet, the definition of ''qualified client'' in the rule could be affected by the amendments. As of August 2021, of the approximately 14,543 investment advisers registered with the Commission, 5,251 (36%)

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[10] Rule 205–3(d) and (e). *See* Investment Adviser Performance Compensation, Investment Advisers Act Release No. 3372 (Feb. 15, 2012) [77 FR 10358 (Feb. 22, 2012)]. Rule 205–3(e) also specifies the methodology and price index on which inflation adjustments must be based.

[11] Order Approving Adjustment for Inflation of the Dollar Amount Tests in Rule 205–3 under the Investment Advisers Act of 1940, Investment Advisers Act Release No. 4421 (June 14, 2016) [81 FR 39985 (June 20, 2016)] (''2016 Order'').

[12] Order Approving Adjustment for Inflation of the Dollar Amount Tests in Rule 205–3 under the Investment Advisers Act of 1940, Investment Advisers Act Release No. 5756 (June 17, 2021) [86 FR 32993 (June 23, 2021)] (''2021 Order''). Both the 2016 Order and the 2021 Order stated that to the extent that contractual relationships were entered into prior to the order's effective date, the adjustments to the dollar amount thresholds would not generally apply retroactively to such contractual relationships, subject to the transition rules of rule 205–3, which are described *infra* footnote 14.

[13] Such orders are published in the **Federal Register**, but are also available on the SEC's website at *www.sec.gov/rules/other.shtml. See, e.g.,* 2021 Order, *supra* footnote 12. Publication of the orders on the website may precede publication in the **Federal Register**.

[14] The effective dates of the adjustments are specified in the ''most recent order'' and are subject to the transition provisions of the rule. *See, e.g.,* 2021 Order, *supra* footnote 12. The transition provisions state, for example, that if a registered investment adviser entered into a contract and satisfied the conditions of rule 205–3 that were in effect when the contract was entered into, the adviser will be considered to satisfy the conditions of the rule; if, however, a natural person or company that was not a party to the contract becomes a party, the conditions of the rule in effect at the time such natural person or company becomes a party will apply to that person or company. *See* rule 205–3(c)(1) through (3).

[15] Rule 205–3(e).

[16] 5 U.S.C. 553(b). The amendments to rule 205–3 do not require analysis under the Regulatory Flexibility Act (''RFA'') 5 U.S.C. 601(2) (for purposes of RFA analysis, the term ''rule'' generally means any rule for which the agency publishes a general notice of proposed rulemaking). In addition, pursuant to the Congressional Review Act, the Office of Information and Regulatory Affairs has designated the amendments to rule 205–3 as not a ''major rule'' as defined by 5 U.S.C. 804(2). *See* 5 U.S.C. 801 *et seq.*

[17] 5 U.S.C. 553(d)). This finding also satisfies the requirements of 5 U.S.C. 808(2), allowing the amendment to rule 205–3 to become effective notwithstanding the requirement of 5 U.S.C. 801 (if a Federal agency finds that notice and public comment are impracticable, unnecessary or contrary to the public interest, a rule shall take effect at such time as the federal agency promulgating the rule determines). Therefore, the amendments to rule 205–3 shall take effect on November 10, 2021.

[18] 44 U.S.C. 3501–3520.

currently report that they are compensated with performance-based fees.[19]

We do not, however, expect that the amendments to rule 205–3 will result in substantial costs or benefits to these market participants. As described above, rule 205–3 currently references specific dollar amount thresholds in the rule's net worth and assets-under-management tests in paragraph (d)(1) and, separately, specifies that these thresholds will be adjusted for the effects of inflation by order of the Commission in paragraph (e). The amendments replace the specific dollar amount thresholds with references to the ''most recent order'' issued by the Commission containing the specific dollar amount thresholds adjusted for inflation, consistent with existing paragraph (e) of the rule. The amendments do not themselves change the dollar amount thresholds used in the definition, and, as a result, will not have any effect on the number of clients that meet the rule's definition of ''qualified client.'' Further, we do not believe the amendments will affect the number of advisers charging clients performance fees. The amendments also update the date from ''May 1, 2016'' to ''May 1, 2026'' in paragraph (e) to indicate when the next adjustment will occur, with future adjustments every five years thereafter, although this update does not reflect any change in process or timing from the existing rule.

The amendments to rule 205–3 could help investment advisers and clients more easily identify the current thresholds in the ''qualified client'' definition to the extent that the text of rule 205–3 is inconsistent with the most recent order issued by the Commission or to the extent that investment advisers and clients are unaware of such inconsistency. Relatedly, the updated date in paragraph (e) may help investment advisers and clients more easily determine approximately when the Commission will next issue an order and set expectations for future changes. These effects could incrementally reduce compliance costs; however, we do not expect any such reductions to be substantial.

Similarly, we do not expect any changes to efficiency, competition, or capital formation in the investment adviser industry as a result of the amendments to rule 205–3. While the amendments may make the identification of ''qualified clients'' incrementally easier by clarifying that the current thresholds in the ''qualified client'' definition may be found in the most recent order issued by the Commission, we do not believe that these changes will substantially affect an adviser's ability to identify ''qualified clients'' or raise capital from such clients.

[19] This analysis is based on adviser responses to Item 5.E.6 of Part 1A on Form ADV. This Item requests that an adviser note whether it receives performance-based fees.

IV. Statutory Authority

The Commission is adopting amendments to rule 205–3 under the Advisers Act pursuant to the authority set forth in section 205(e) of the Investment Advisers Act of 1940 [15 U.S.C. 80b–5(e)].

List of Subjects in 17 CFR Part 275

Reporting and recordkeeping requirements, Securities.

Text of Rules

For the reasons set out in the preamble, title 17, chapter II of the Code of Federal Regulations is amended as follows:

PART 275—RULES AND REGULATIONS, INVESTMENT ADVISERS ACT OF 1940

■ 1. The authority citation for part 275 continues to read, in part, as follows:

Authority: 15 U.S.C. 80b–2(a)(11)(G), 80b–2(a)(11)(H), 80b–2(a)(17), 80b–3, 80b–4, 80b–4a, 80b–6(4), 80b–6a, and 80b–11, unless otherwise noted.

* * * * *

Section 275.205–3 is also issued under 15 U.S.C. 80b–5(e).

* * * * *

■ 2. Section 275.205–3 is amended by:

■ a. Revising paragraphs (d)(1)(i) and (d)(1)(ii)(A) introductory text;

■ b. Adding paragraph (d)(5); and

■ c. Revising paragraph (e) introductory text.

The revisions and addition read as follows:

§ 275.205–3 Exemption from the compensation prohibition of section 205(a)(1) for investment advisers.

* * * * *

(d) * * *

(1) * * *

(i) A natural person who, or a company that, immediately after entering into the contract has, under the management of the investment adviser, at least the applicable dollar amount specified in the most recent order;

(ii) * * *

(A) Has a net worth (together, in the case of a natural person, with assets held jointly with a spouse) of more than the applicable dollar amount specified in the most recent order. For purposes of calculating a natural person's net worth:

* * * * *

(5) The term *most recent order* means the most recently issued Commission order in accordance with paragraph (e) of this section and as published in the **Federal Register**.

(e) *Inflation adjustments.* Pursuant to section 205(e) of the Act, the dollar amounts referenced in paragraphs (d)(1)(i) and (d)(1)(ii)(A) of this section shall be adjusted, by order of the Commission, issued on or about May 1, 2026, and approximately every five years thereafter. The adjusted dollar amounts established in such orders shall be computed by:

* * * * *

By the Commission.

Dated: November 4, 2021.

Vanessa A. Countryman,

Secretary.

[FR Doc. 2021–24525 Filed 11–9–21; 8:45 am]

BILLING CODE 8011–01–P

DEPARTMENT OF THE TREASURY

Alcohol and Tobacco Tax and Trade Bureau

27 CFR Part 9

[Docket No. TTB–2020–0002; T.D. TTB–174; Ref: Notice No. 187]

RIN 1513–AC54

Establishment of the Verde Valley Viticultural Area

AGENCY: Alcohol and Tobacco Tax and Trade Bureau, Treasury.

ACTION: Final rule; Treasury decision.

SUMMARY: The Alcohol and Tobacco Tax and Trade Bureau (TTB) establishes the approximately 200-square mile ''Verde Valley'' viticultural area (AVA) in Yavapai County, Arizona. The Verde Valley viticultural area is not located within any other established viticultural area. TTB designates viticultural areas to allow vintners to better describe the origin of their wines and to allow consumers to better identify wines they may purchase.

DATES: This final rule is effective December 10, 2021.

FOR FURTHER INFORMATION CONTACT: Karen A. Thornton, Regulations and Rulings Division, Alcohol and Tobacco Tax and Trade Bureau, 1310 G Street NW, Box 12, Washington, DC 20005; phone 202–453–1039, ext. 175.

SUPPLEMENTARY INFORMATION: