ADMINISTRATIVE LAW — JUDICIAL REVIEW OF AGENCY RULEMAKING — DISTRICT OF COLUMBIA CIRCUIT VACATES SECURITIES AND EXCHANGE COMMISSION'S "HEDGE FUND RULE." — *Goldstein v. SEC*, 451 F.3d 873 (D.C. Cir. 2006).

Even the worst-run companies can take years to lose six billion dollars. In September 2006, the hedge fund Amaranth Advisors lost that sum in one week.[1] The evident susceptibility of hedge funds to losses of such scope and suddenness, beginning with the 1998 collapse of Long-Term Capital Management[2] (LTCM), has increasingly drawn the attention of the SEC. Responding in part to the LTCM crisis, the SEC promulgated a new regulation in 2004 that required hedge fund managers to register pursuant to the Investment Advisers Act of 1940[3] (IAA). As part of this new "Hedge Fund Rule,"[4] the SEC also narrowed the reach of a key IAA exemption. The Act exempts fund managers from registration if they have fewer than fifteen "clients,"[5] a term the Hedge Fund Rule interpreted to include not only the funds themselves but also individuals. As a result, previously exempt managers suddenly found themselves above the fifteen-client threshold.[6] Under longstanding administrative law doctrine, this change should have survived legal challenge: reviewing courts cannot substitute their own construction of a statute for an agency's reasonable interpretation[7] and must defer to reasoned policy changes.[8] Recently, in *Goldstein v. SEC*,[9] the D.C. Circuit invalidated the Hedge Fund Rule as an instance of arbitrary rulemaking by the SEC.[10] In so holding, the

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[1] *See* Daniel P. Collins, *Deconstructing Amaranth*, FUTURES, Nov. 2006, at 18. The loss resulted from a single trader's "use [of] borrowed money to double-down" on natural-gas contract positions. Ann Davis et al., *What Went Wrong at Amaranth*, WALL ST. J., Sept. 20, 2006, at C1; *see also* Henny Sender & Gregory Zuckerman, *Street Sleuth: Amaranth Natural-Gas Losses May Have Far-Reaching Effect*, WALL ST. J., Sept. 19, 2006, at C3 (reporting the view of an industry insider that "[t]o produce those kinds of losses means borrowing about $8 for every $1 invested" (internal quotation mark omitted)).

[2] Long-Term Capital Management had more than $125 billion in assets under management. It grew rapidly by entering into highly leveraged foreign currency arbitrages. In late 1998, the fund became overextended in a position on Russian currency and collapsed, nearly triggering a nationwide financial crisis. *See* ROGER LOWENSTEIN, WHEN GENIUS FAILED: THE RISE AND FALL OF LONG-TERM CAPITAL MANAGEMENT (2000).

[3] Investment Advisers Act of 1940, 15 U.S.C. § 80b-1 to -21 (2000).

[4] Registration of Certain Hedge Fund Advisers, Investment Advisers Release No. 2333, 69 Fed. Reg. 72,054 (Dec. 10, 2004) (codified at 17 C.F.R. pts. 275, 279 (2006)).

[5] IAA § 203, 15 U.S.C. § 80b-3(b)(3).

[6] This change greatly increased agency oversight, allowing the SEC to undertake a census of fund managers and to require advisers both to open their records to the SEC and to forgo performance fees for certain clients. *See* Goldstein v. SEC, 451 F.3d 873, 877 & n.3 (D.C. Cir. 2006).

[7] Chevron U.S.A. Inc. v. Natural Res. Def. Council, Inc., 467 U.S. 837, 844 (1984).

[8] *See* Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co., 463 U.S. 29 (1983).

[9] 451 F.3d 873.

[10] *Id.* at 884.

court not only departed from its tradition of deferring to agency expertise, but also failed to advance the purposes underlying the IAA. Further, the court missed an opportunity to allow agencies greater substantive rulemaking flexibility in areas in which parties have the ability and incentives to escape regulation.

In 1985, the SEC promulgated a "Safe Harbor Rule"[11] that effectively excused from registration hedge fund managers under the IAA's fifteen-client limit by counting a hedge fund, and not each individual investor, as one client.[12] Almost two decades later, citing several changes in the economy — such as the growth in the number and importance of hedge funds, an increase in fraud cases involving fund managers, and a greater exposure of retail investors to the risks of hedge fund investing[13] — the SEC revisited the issue in a new round of notice-and-comment rulemaking. With two members dissenting, the SEC promulgated the final Hedge Fund Rule in December 2004.[14] An investment adviser named Phillip Goldstein[15] immediately challenged the rule in the D.C. Circuit.[16]

The D.C. Circuit vacated the Hedge Fund Rule and remanded. Writing for a unanimous panel, Judge Randolph[17] held that the SEC's departure from its earlier Safe Harbor Rule was invalid as an arbitrary action that conflicted with the purposes of the IAA.[18] Judge Randolph began his opinion by providing an overview of hedge funds, noting the difficulty of even defining what a hedge fund is.[19] Because

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[11] Definition of "Client" for Certain Purposes, Investment Advisers Release No. 956, 50 Fed. Reg. 8740 (Mar. 5, 1985) (codified at 17 C.F.R. § 275.203(b)(3)-1).

[12] *Goldstein*, 451 F.3d at 880.

[13] *See id.* at 877; Brief of Respondent at 9–11, 451 F.3d 873 (No. 04-1434), 2005 WL 1636146.

[14] Registration of Certain Hedge Fund Advisers, Investment Advisers Release No. 2333, 69 Fed. Reg. 72,054 (Dec. 10, 2004) (codified at 17 C.F.R. pts. 275, 279 (2006)).

[15] Mr. Goldstein was joined in his court challenge by an investment advisory firm he co-owned and a hedge fund for which the firm served as investment adviser. He had strenuously objected during the notice-and-comment period. *See* Letter from Phillip Goldstein, President, Opportunity Partners L.P., to the SEC (Sept. 10, 2004), *available at* http://www.sec.gov/rules/proposed/s73004/pgoldstein091004.pdf (making legal objections to the SEC's proposed rule in the form of an imagined conversation with "Humpty Dumpty's great great grandson, Bumpty Dumpty[,] . . . a senior staff attorney at the SEC").

[16] The IAA provides for direct challenges in the D.C. Circuit. IAA § 213, 15 U.S.C. § 80b-13(a) (2000).

[17] Judge Randolph was joined by Judge Edwards and Judge Griffith.

[18] *Goldstein*, 451 F.3d at 883–84.

[19] *Id.* at 874. Although there is no universal definition, the term is commonly used to describe "any pooled investment vehicle that is privately organized, administered by professional investment managers, and not widely available to the public." *Id.* at 875 (quoting PRESIDENT'S WORKING GROUP ON FIN. MKTS., HEDGE FUNDS, LEVERAGE, AND THE LESSONS OF LONG-TERM CAPITAL MANAGEMENT 1 (1999)) (internal quotation marks omitted); *see also* Barry Eichengreen & Donald Mathieson, *Hedge Funds and Financial Markets: Implications for Policy*, *in* BARRY EICHENGREEN ET AL., HEDGE FUNDS AND FINANCIAL MARKET DYNAMICS 2, 2 (1998) ("Hedge funds can be defined as eclectic investment pools, organized as pri-

of their structure, hedge funds historically have been subject to minimal oversight. Most can engage in investing behavior, such as trading on margin and short selling, to which traditional entities, such as mutual funds, have limited access.[20] Moreover, unlike traditional funds, hedge funds can "remain secretive about their positions and strategies, even to their own investors."[21]

The court considered whether, under the Administrative Procedure Act[22] (APA), the SEC's redefinition of "client" was "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with the law."[23] The petitioners argued primarily that the new rule misinterpreted "client" as used in section 203(b)(3) of the IAA.[24] The Commission responded that the statute's use of the term was ambiguous,[25] triggering the deferential standard outlined by the Supreme Court in *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*[26]

The court rejected the SEC's argument. Although the IAA does not define "client,"[27] this fact alone, the court held, did not render the term ambiguous, and even if the word were open to several meanings, "it scarcely follow[ed] that Congress ha[d] authorized the SEC to choose *any* one of those meanings."[28] The court found the SEC's construction unreasonable in light of the court's own interpretation of the term. Judge Randolph pointed to several factors, such as the IAA's definition of "investment adviser" as one who "engages in the business of advising others . . . as to the value of securities or as to the advisability of investing in . . . securities."[29] The court also noted the SEC's past view, articulated in the Safe Harbor Rule, by which "client" was

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vate partnerships . . . whose managers are paid on a fee-for-performance basis. Their prospectuses and legal status place few restrictions on their portfolios and transactions.").

[20] *See Goldstein*, 451 F.3d at 875; LOWENSTEIN, *supra* note 2, at 24.

[21] *Goldstein*, 451 F.3d at 875.

[22] 5 U.S.C. §§ 551–559, 701–706 (2000 & Supp. IV 2004).

[23] *Id.* § 706(2)(a); *see also* Citizens To Preserve Overton Park, Inc. v. Volpe, 401 U.S. 402, 413–14 (1971). Because the IAA does not expressly preclude application of the APA, *see* IAA § 213, 15 U.S.C. § 80b-13(a) (2000), it was appropriate to use the APA standard of review, 5 U.S.C. § 559.

[24] *See Goldstein*, 451 F.3d at 878 (citing 14 U.S.C. § 80b-3(b)(3)); Brief of Petitioners at 35–44, *Goldstein* (No. 04-1434), 2005 WL 1666937.

[25] *See Goldstein*, 451 F.3d at 878.

[26] 467 U.S. 837, 842–43 (1984).

[27] *Goldstein*, 451 F.3d at 878. Past legislative and judicial pronouncements also left the issue open. *See id.* at 878–79 (discussing the 1970 and 1980 amendments to the IAA and *Abrahamson v. Fleschner*, 568 F.2d 862 (2d Cir. 1977)).

[28] *Id.* at 878. This statement seems to implicate the underlying justification for *Chevron*: ambiguity signals congressional intent to delegate to agencies. *See* Smiley v. Citibank (S.D.), N.A., 517 U.S. 735, 740–41 (1996) ("We accord deference . . . because of a presumption that Congress, when it left ambiguity in a statute meant for implementation by an agency, . . . desired the agency (rather than the courts) to possess whatever degree of discretion the ambiguity allows.").

[29] *Goldstein*, 451 F.3d at 879 (quoting 15 U.S.C. § 80b-2(11) (2000)) (internal quotation mark omitted).

defined to mean "the limited partnership," not the individual partners.[30] In addition, the court identified *Lowe v. SEC*,[31] a case holding that publishers of financial newsletters were not "investment advisers" under the IAA,[32] as presenting a significant obstacle to the SEC's reading.[33] The Supreme Court in *Lowe* reasoned that the IAA's reference to "clients" indicated "the kind of fiduciary relationship the Act was designed to regulate."[34] This relationship led Judge Randolph to conclude that the SEC's construction came "close to violating the plain language of the statute": an adviser owes fiduciary duties to the fund, not to individual investors, and the SEC did not explain why "client" means one thing with regard to fiduciary duties and another when determining the fund's obligation to register.[35]

The court further concluded that because the SEC had failed to provide a plausible reason for its abandonment of the Safe Harbor Rule, the Commission's new position was arbitrary.[36] According to the court, the SEC had not explained how the relationship between investors and advisers had changed, or how the new relationship justified treating investors as clients.[37] Further, the SEC had failed to connect its stated view of Congress's intent — limiting the IAA's application to funds that were "national in scope" — to the SEC's new interpretation of the fifteen-client limit because the number of a fund's individual clients gives little indication of the scope of its activities.[38]

In vacating the Hedge Fund Rule, the D.C. Circuit reached an outcome at odds both with settled administrative law and with the IAA's purposes. More importantly, the court missed an opportunity to adapt its jurisprudence to a rulemaking context that may be unique to the financial sector, in which systemic risk is high and regulated parties face strong incentives — and have substantial power — to avoid regulation. Whereas most parties cannot easily escape environmental or health regulations, financial actors can contract around agency action. And whereas parties in other sectors, by avoiding regulation, primarily

[30] *Id.* at 880 (citing 17 C.F.R. § 275.203(b)(3)-1(a)(2) (2006)).

[31] 472 U.S. 181 (1985).

[32] *Id.* at 211.

[33] *Goldstein*, 451 F.3d at 880.

[34] *Id.* (quoting *Lowe*, 472 U.S. at 201 n.45) (internal quotation marks omitted).

[35] *Id.* at 881–82.

[36] *See id.* at 882–84. A court cannot deny *Chevron* deference because of an agency's inconsistent position, but it can find an unexplained inconsistency arbitrary and capricious. Nat'l Cable & Telecomms. Ass'n v. Brand X Internet Servs., 125 S. Ct. 2688, 2699 (2005). *But see* ALFRED C. AMAN, JR. & WILLIAM T. MAYTON, ADMINISTRATIVE LAW § 13.8.3, at 500 (2d ed. 2001) (suggesting that, in practice, courts rarely defer when they find an agency has been inconsistent).

[37] *Goldstein*, 451 F.3d at 882.

[38] *Id.* at 883.

avoid compliance costs, financial actors can realize far greater benefits.[39] Such circumstances call for greater agency flexibility.

The court's refusal to accept the SEC's reading of the IAA was improper under *Chevron*. *Chevron* instructs courts to defer to reasonable agency interpretations of ambiguous terms in a statute the agency is charged with administering.[40] The *Chevron* Court stressed that a reviewing court should not substitute its own judgment for that of the agency: "[T]he question . . . is whether the agency's answer is based on a permissible construction of the statute."[41] An agency's mere adoption of an interpretation that conflicts with its earlier position does not suffice to create an exception to this principle.[42] The *Goldstein* court, rather than substituting its own reading, should have deferred to the SEC's: the IAA is ambiguous with respect to who should be counted as a client of an investment firm, and the SEC's interpretation comported with the text of the IAA.[43]

The IAA's history and purpose also support the SEC's construction. As the Supreme Court has noted, Congress passed the IAA as "the last in a series of Acts designed to eliminate certain abuses in the securities industry, abuses which were found to have contributed to the stock market crash of 1929."[44] To meet this goal, the statutes shared the "fundamental purpose" of substituting "a philosophy of full disclosure for the philosophy of *caveat emptor*."[45] The Court has thus held

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[39] As unregulated actors, hedge funds can engage in more (and riskier) trading strategies, earning profits beyond those stemming from avoiding the direct costs of compliance.

[40] *See* K Mart Corp. v. Cartier, Inc., 486 U.S. 281, 291–92 (1988).

[41] Chevron U.S.A. Inc. v. Natural Res. Def. Council, Inc., 467 U.S. 837, 843 (1984).

[42] *See* Smiley v. Citibank (S.D.), N.A., 517 U.S. 735, 740–41 (1996).

[43] The court rested its holding to the contrary on a "conflict" between the SEC's construction and a separate section of the statute, as well as on the *Lowe* case (which was not directly on point). The Hedge Fund Rule, by its own terms, did not alter the fiduciary duty between a hedge fund manager and the fund's investors. It stated that, solely for purposes of registration, certain hedge funds had to count each investor as a client; it did not require that the funds treat each investor as a client. *See* 17 C.F.R. § 275.203(b)(3)-2(a) (2006). Indeed, the SEC expressly disclaimed such an intent. *See* Brief of Respondent, *supra* note 13, at 18. The court stated that it "ordinarily presume[s] that the same words used in different parts of a statute have the same meaning," *Goldstein*, 451 F.3d at 882, but this presumption derives from a desire to respect the intent of Congress and is rebuttable, *see, e.g.*, Helvering v. Stockholms Enskilda Bank, 293 U.S. 84, 87 (1934). Here, the history and purpose of the IAA point to a congressional intent to use the number of a fund's clients to measure its scope. Fiduciary duties should be immaterial to such a determination.

[44] SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 186 (1963). One factor that contributed to the 1929 crash was investors' significant use of leverage. Interestingly, some current abuses mirror Depression-era practices, differing only in degree. *Compare* JOHN KENNETH GALBRAITH, A SHORT HISTORY OF FINANCIAL EUPHORIA 76–77 (1993) (reporting pre-Depression traders' use of leverage at a nine-to-one ratio), *with* Sender & Zuckerman, *supra* note 1 (reporting Amaranth's use of leverage at an eight-to-one ratio), *and* Franklin R. Edwards, *Hedge Funds and the Collapse of Long-Term Capital Management*, 13 J. ECON. PERSP. 189, 198 (1999) (noting that LTCM's failure was magnified by its dramatic use of leverage).

[45] *Capital Gains Research Bureau*, 375 U.S. at 186.

that Congress intended the IAA "to be construed like other securities legislation 'enacted for the purpose of avoiding frauds,' not technically and restrictively, but flexibly, to effectuate its remedial purposes."[46] Viewed against this backdrop, the Hedge Fund Rule's redefinition of an ambiguous term in the IAA to allow the SEC better to "respond to, initiate, and take remedial action on complaints against fraudulent advisers"[47] should be a permissible action.

Even were the *Goldstein* court correct in vacating the Hedge Fund Rule, the outcome of the case is flawed from a policy standpoint. The court missed an opportunity to advance administrative law in the area of agency rulemaking flexibility. Courts have traditionally recognized the need for agency flexibility in choosing methods for setting policy[48] and in revisiting informal interpretive rules.[49] This is particularly true when Congress may be unable to predict future regulatory needs.[50] An agency that seeks to revisit an existing rule, however, faces an added barrier: it must justify not only the new rule, but also its decision to change the old one.[51] Even plausible justifications run a high risk of being found legally unsatisfactory.[52] *Goldstein* is a good example: the court acknowledged industry changes — such as LTCM's 1998 collapse — between the 1985 Safe Harbor Rule and the 2004 Hedge Fund Rule but still rejected the new rule.[53]

The context in which the SEC promulgated the Hedge Fund Rule demonstrates the need for flexibility in agency rulemaking. The af-

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[46] *Id.* at 195 (quoting 3 J.G. SUTHERLAND, STATUTES AND STATUTORY CONSTRUCTION 382 (3d ed. 1943)).

[47] *Goldstein*, 451 F.3d at 876.

[48] *See, e.g.*, SEC v. Chenery Corp. (*Chenery II*), 332 U.S. 194 (1947) (stressing the need for agency flexibility to respond to unforeseen circumstances and holding that the agency was authorized to use adjudication to accomplish results similar to rulemaking); *see also* NLRB v. Bell Aerospace Co., 416 U.S. 267 (1974) (same).

[49] *See* Jon Connolly, Note, Alaska Hunters *and the D.C. Circuit: A Defense of Flexible Interpretive Rulemaking*, 101 COLUM. L. REV. 155 (2001). For a discussion of interpretive rules, see Matthew C. Stephenson, *The Strategic Substitution Effect: Textual Plausibility, Procedural Formality, and Judicial Review of Agency Statutory Interpretations*, 120 HARV. L. REV. 528, 531 (2006).

[50] *See, e.g.*, *Chenery II*, 332 U.S. 194. Agency expertise may also lead to better predictions of and responses to industry changes.

[51] *See* Nat'l Cable & Telecomms. Ass'n v. Brand X Internet Servs., 125 S. Ct. 2688, 2699 (2005); AMAN & MAYTON, *supra* note 36, § 13.10.4, at 519.

[52] Some Justices have argued for a more permissive approach. *See* FDA v. Brown & Williamson Tobacco Corp., 529 U.S. 120, 188–89 (2000) (Breyer, J., dissenting) (arguing that even a change in presidential administration should be enough to justify an agency's policy change); Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co., 463 U.S. 29, 59 (1983) (Rehnquist, J., concurring in part and dissenting in part) (same). Despite the attractiveness of this argument, courts still demand a greater showing from agencies under these circumstances.

[53] *See Goldstein*, 451 F.3d at 877, 883.

fected managers oversee rapidly growing asset pools[54] and increasingly engage in unorthodox strategies[55] that, as the *Goldstein* court recognized, can be kept secret from investors.[56] More importantly, hedge funds by their nature create significant risk to the economy.[57] This risk flows from a substantial incentive of funds and their managers to avoid regulation: the need for secrecy.[58] Although any arbitrageur will seek to keep its trading strategies secret,[59] hedge funds have more assets under management and greater access to credit, magnifying the risk created by secrecy. Further, fund managers have the power to modify the terms of their relationships with investors contractually.[60]

Recognizing a need for greater flexibility in some contexts need not lead to "abdication" by a reviewing court.[61] Ideally, the court would look to the overall context in which an agency acted, including the risk that the agency sought to address and the status of legislative solutions

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[54] In 2003, the SEC reported estimates of "approximately 6,000 hedge funds" in the United States "with approximately $600 billion in assets under management." SEC, IMPLICATIONS OF THE GROWTH OF HEDGE FUNDS 1 n.2 (2003), *available at* http://www.sec.gov/news/studies/hedgefunds0903.pdf. A 1998 report estimated the number at 914, with $110 billion under management. *See* BARRY EICHENGREEN & DONALD MATHIESON, HEDGE FUNDS: WHAT DO WE REALLY KNOW? 6 (1999). A recent media report estimated the number at "more than 3,000," managing "more than $1 trillion." Editorial, *Targeting Hedge Funds*, WALL ST. J., Oct. 31, 2006, at A18. These numbers are only estimates. *See* LESLIE RAHL, HEDGE FUND RISK TRANSPARENCY 169 (2003). The wide range of figures demonstrates either the deep uncertainty involved in estimating this market, the tremendous growth of funds in the last seven years, or that both propositions are true.

[55] *See, e.g.*, JAMES ALTUCHER, SUPERCASH: THE NEW HEDGE FUND CAPITALISM 9–20 (2006) (detailing new strategies in which hedge funds have engaged, including subprime auto finance, real estate lending, and purchasing taxi medallions); *Don't Hedge Funds In*, FIN. TIMES (London), Oct. 17, 2006, at 16 ("Some hedge funds are becoming more like banks.").

[56] *See Goldstein*, 451 F.3d at 875.

[57] Hedge funds played a role in many recent financial crises. *See* EICHENGREEN & MATHIESON, *supra* note 54, at 1 (reporting that "[h]edge funds were implicated" in crises in 1992 (exchange rates), 1994 (international bond markets), 1997 (Asian markets), and 1998 (Asian currency crisis)); *see also* Eichengreen & Mathieson, *supra* note 19, at 14–23. Because of the expertise of the SEC and other agencies, their efforts to address this type of systemic risk are likely to be more successful than those of Congress.

[58] *See* Donald MacKenzie, *How a Superportfolio Emerges: Long-Term Capital Management and the Sociology of Arbitrage*, *in* THE SOCIOLOGY OF FINANCIAL MARKETS 62, 71–72 (Karin Knorr Cetina & Alex Preda eds., 2005) (noting LTCM's efforts to keep its strategy secret to deter imitators).

[59] *See* JOHN C. COX & MARK RUBINSTEIN, OPTIONS MARKETS 128 (1985) (noting that a known arbitrage possibility will draw investors, eliminating the profit opportunity).

[60] It may be impossible, for example, to avoid an FAA regulation that bars pilots from operating commercial aircraft after age sixty, *see* Yetman v. Garvey, 261 F.3d 664, 679 (7th Cir. 2001), but a hedge fund manager need only alter her standard contract with investors, *see* GREGORY J. NOWAK, HEDGE FUND AGREEMENTS LINE BY LINE (2004).

[61] *See* Ethyl Corp. v. EPA, 541 F.2d 1, 69 (en banc) (D.C. Cir. 1976) (Leventhal, J., concurring). Nor should such an approach grant agencies unlimited power to change their positions: courts can restrain agency flexibility through related doctrines such as reliance. *See* AMAN & MAYTON, *supra* note 36, § 13.8.4, at 502. A reliance limitation would also address fairness concerns.

to the problem,[62] as well as the agency's expertise and the nature of the authority Congress originally delegated to it. Such a totality-of-the-circumstances analysis[63] would comport with *Chevron* because the reviewing court would not be substituting its own judgment about the meaning of the statute. Instead, the delegation, coupled with other factors, would color the court's determination of how much deference is warranted. In an analysis of an agency's inconsistent position, these factors would also affect how much latitude a court should afford the agency's explanation. Rather than focusing only on narrow issues such as the agency's justification for instituting a change,[64] the court would adopt a wider view of "permissible construction" that respects the tradition of deference to agency expertise and congressional delegation.

Ideally, the solution to the challenges that hedge funds present would come from Congress. However, because of the many forms that these funds take and their incentives to embrace secrecy and avoid regulation, legislation will almost certainly fail to anticipate future trends. Administrative regulation is a viable solution. The Hedge Fund Rule was a modest first step, aimed mainly at gathering information to counter the threat of fraudulent activity[65] and to assess the need for future action. The *Goldstein* case left an entire industry without even this modest progress toward oversight. The Amaranth debacle, occurring less than three months after the court handed down its opinion, illustrates the dangers that motivated the rule in the first place, and the need for a doctrine of administrative law that recognizes the importance of agency flexibility in meeting the goals that Congress has set.

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[62] Congress considered a bill requiring funds to register with the Federal Reserve, *see* Hedge Fund Disclosure Act, H.R. 2924, 106th Cong. (1999), but the bill died in committee.

[63] Although this test is similar to the *Skidmore* factors that courts apply when *Chevron* deference does not attach, *see* United States v. Mead Corp., 533 U.S. 218, 234–35 (2001); Skidmore v. Swift & Co., 323 U.S. 134, 140 (1944), it would not affect the validity of the agency's interpretation in the absence of *Chevron* deference. The test would instead apply to the question of whether the agency should receive heightened deference in the first place.

[64] In *Goldstein*, for example, the court stressed the need for a showing that the relationship between advisers and clients had changed, *see Goldstein*, 451 F.3d at 882, but this approach asks the wrong question. In *Chevron*, the Court examined the EPA's change by looking to the nature of the congressional delegation, the goals underlying that delegation, and the reasonableness of the agency's construction in attempting to meet those goals. In short, the relevant change is that of the overall regulatory context.

[65] *See generally* Paul N. Roth, *SEC Investigation of Hedge Funds; Enforcement Actions*, *in* HEDGE FUNDS: HOT REGULATORY & OPERATIONAL ISSUES 65, 71–81 (PLI Corp. Law and Practice Course Handbook Series No. B-1365, 2003), WL 1365 PLI/Corp 65 (reporting a series of recent SEC enforcement actions against fraudulent fund managers).