

## SEC Proposes Rules to Enhance Private Fund Disclosures and Prohibit Certain Private Fund Adviser Activities

February 10, 2022

On February 9, 2022, the Securities and Exchange Commission (the “*Commission*”) voted 3 to 1 to propose new and amended rules under the Investment Advisers Act of 1940 (the “*Advisers Act*”) to require advisers to private funds to provide additional disclosures to investors in such funds, prohibit certain types of preferential treatment to investors and impose new requirements related to fund audits, books and records and adviser-led secondary transactions. Specifically, the Commission is proposing to:

- Require private fund advisers to provide investors with quarterly statements including information about fund performance, fees and expenses;
- Require private fund advisers to obtain an annual audit of each advised fund conducted by an independent public accountant subject to regular inspection by the Public Company Accounting Oversight Board;
- Require private fund independent public accountants to notify the Commission upon issuing an audit report to a fund that contains a modified opinion or upon its resignation, termination, or removal from consideration of being reappointed as a fund’s auditor;
- Require private fund advisers, in connection with an adviser-led secondary transaction, to obtain and distribute to investors a fairness opinion and a written summary of certain material relationships between the adviser and the opinion provider;
- Prohibit private fund advisers from engaging in certain activities and practices described by the Commission as “contrary to the public interest and the protection of investors,” including:
  - Charging certain fees and expenses to a private fund or its portfolio investments, such as fees for unperformed services (e.g., accelerated monitoring fees) and fees associated with an examination or investigation of the adviser by any governmental or regulatory authority;
  - Seeking reimbursement, indemnification, exculpation, or limitation of its liability for certain conduct, including breaches of fiduciary duties;
  - Reducing the amount of an adviser clawback by the amount of actual, potential or hypothetical taxes;
  - Charging fees or expenses (including broken deal expenses) related to an actual or proposed portfolio investment on a non-pro rata basis; and
  - Borrowing or receiving an extension of credit from a private fund client;
- Prohibit private fund advisers from providing preferential liquidity or transparency terms to certain investors (such as through a side letter agreement) that may have a material negative effect on other investors;
- Prohibit private fund advisers from providing all types of preferential treatment to certain investors and not others unless current and prospective investors receive disclosure specifically describing the preferential treatment (i.e., general disclosure about the ability to enter into side letters in the fund’s offering documents would not appear to satisfy the requirement);

- Require registered advisers, including those that do not advise private funds, to document the annual review of their compliance policies and procedures in writing.

The full text of the proposal, including instructions on how to submit comments, is available [here](#). The rule proposal follows an increased focus on private funds and their advisers by the Commission and its staff, including a recent [Risk Alert](#) issued by the Division of Examinations detailing deficiencies identified during examinations of private fund advisers. The Commission's new proposal represents the most significant recent effort to regulate the \$18 trillion private fund industry. The Commission will accept public comments on the proposal until the later of 30 days following its publication in the Federal Register or April 11, 2022.

## For More Information

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If you would like further information concerning the matters discussed in this Client Alert, please contact one of the attorneys listed below, any member of the Investment Management Group or your regular Chapman contact, or visit us online at [chapman.com](http://chapman.com).

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