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SIGNIFICANT PROPOSED SEC RULES FOR ADVISERS TO PRIVATE FUNDS

The proposed SEC rules would affect all advisers to private funds. If adopted as proposed, private fund advisers would be prohibited from, among other things, (i) charging private funds for certain costs, fees and expenses, (ii) agreeing to indemnification provisions for negligence or a breach of fiduciary duty, and (iii) granting certain preferential redemption terms or information rights. Private fund advisers also would be subject to prescriptive quarterly reporting, be required to have annual private fund audited financial statements prepared, and be required to obtain fairness opinions for adviser-led secondary transactions. The proposed rulemaking reflects sweeping new proposed requirements for the private fund industry and has garnered significant industry comment.

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The Securities and Exchange Commission proposed new rules (the “Proposed Rules”) under the Investment Advisers Act of 1940 (the “Advisers Act”) on February 9, 2022.¹ The Proposed Rules would prohibit private fund advisers from charging private funds certain regulatory or compliance costs, fees, and expenses on a non-pro rata basis, and certain accelerated monitoring fees. Private fund advisers also would be prohibited from agreeing to indemnification and exculpation provisions for negligence or a breach of fiduciary duty. Advisers would be prohibited from granting preferential terms to private fund investors regarding redemption rights and information about portfolio holdings or

exposures that have a material negative effect on other investors. Private fund advisers would also be subject to prescriptive quarterly reporting. In addition, advisers would be prohibited from borrowing assets or receiving an extension of credit from private fund clients and from reducing the amount of any adviser clawback by the amount of certain taxes. Moreover, the Proposed Rules would require registered private fund investment advisers to have annual audited financial statements prepared for private funds and mandate fairness opinions for adviser-led secondary transactions. All registered investment advisers, not only advisers to private funds, would be required to document their annual compliance review in writing. Finally, the SEC proposed amendments to Rule 204-2 under the Advisers Act to impose recordkeeping requirements related to the Proposed Rules. These proposals are the subject of this article.

¹ *Private Fund Advisers; Documentation of Registered Investment Adviser Compliance Reviews*, Advisers Act Release No. 5955 (Feb. 9, 2022) (the “Proposing Release”), available at <https://www.sec.gov/rules/proposed/2022/ia-5955.pdf>.

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