

New SEC Rules Simplified - Know how it can impact you as a fund manager

Introduction

The Securities and Exchange Commission (SEC) adopted new rules and amendments on August 23, 2023, to the Investment Advisers Act of 1940, which will impact private fund advisers in the US. SEC has rolled out the new rules and amendments with the intent to enable increased transparency, efficiency, and competition in the private funds market

Overview of Rules

Rules applicable to only SEC Registered Investment Advisers

Quarterly statements

- Registered fund advisers will be required to provide quarterly statements to investors around fund performance, fees, and expenses in a standardized format

Audit requirements

- Registered fund advisers will be required to submit to their investors, the audited financial statements on an annual basis and upon the liquidation of the fund

GP-led secondaries

- For secondary transactions, advisers must obtain a valuation opinion from an independent provider and share it with the fund investors

Recordkeeping and compliance

- The books and records rules have also been revised, requiring fund advisers to keep records relating to the new rules concerning quarterly statements, annual audits, fairness or valuation opinions, etc

Rules applicable to all Advisers regardless of SEC registration status

Restricted activities

- All Fund managers will be limited from engaging in below listed activities without investor disclosure, or in some cases, investor consent

Restricted Activity	Permitted	Implementation Guidance
Charging or allocating fees associated with regulatory, compliance and examination expenses	With subsequent disclosure	Disclose the amount of such fees to investors within 45 days after the end of the fiscal quarter (90 days after FYE)
Reducing the amount of any performance, compensation clawback by actual, potential or hypothetical taxes	With subsequent disclosure	Disclosure to include the total amount of the adviser clawback, both before and after the clawback reduction
Charging or allocating fees associated with an investigation of the adviser or its related persons	With informed consent	Each fee or expense item must be shown as a distinct line and described in relation to the relevant investigation
Charging or allocating fees and expenses related to an investigation that results or has resulted in Sanction	Prohibited outright	Any fees or expenses associated with an investigation resulting in a sanction must be refunded
Charging or allocating fees and expenses related to a portfolio investment on a non-pro rata basis	With advance disclosure	Disclosure must include a description of how the non-pro rata charge or allocation is fair and equitable
Borrowing money, securities, private fund assets, receiving a loan or extension of credit, from a private fund client	With informed consent	Consent must be accompanied by disclosure describing the material terms of the borrowing

Preferential Treatment

- Prohibits all private fund advisers from providing preferential treatment to investors regarding redemptions and information, if such treatment would have a material, negative effect on other investors



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From when the rules will come into effect?

Rule Name	Private Fund AUM >=\$1.5Bn	Private Fund AUM <=\$1.5Bn
Quarterly Statements	18 Months	18 Months
Audit Requirement	18 Months	18 Months
GP-led Secondaries	12 Months	18 Months
Restricted Activities	12 Months	18 Months
Preferential Treatment	12 Months	18 Months
Recordkeeping & Compliance	60 Days	60 Days

Exception

- The new rules will not be applicable to advisers with a place of business outside of US with respect to their non-U.S. clients (regardless of whether they have U.S. investors)

What it means for PE Fund Advisors?

- **Increased compliance & paperwork:** New rules will increase the reporting, recordkeeping, and disclosure requirements. This will result in expanded SEC examination and oversight of compliance programs
- **Increase in cost of capital:** Private market capital will inevitably become more expensive and compliance expenses will rise as a result of the SEC dictating the format and method of compliance
 - Small and emerging funds will be disproportionately affected since they have less money to dedicate to compliance
 - An increase in the cost of investing capital would also affect early-stage startups and other small, privately held companies' capacity to raise funds
- **Legacy status for prior contracts:** Since the changes are effective at the level of the adviser, it could have possibly warranted in re-negotiation of governing agreements of existing funds
 - To avoid this, SEC has adopted legacy status provisions applicable to certain restricted activities and preferential treatment provisions
 - Such legacy status will apply to those governing agreements entered into in writing prior to the compliance date and with respect to funds that have commenced operations as of the compliance date
- **Status Quo:** Several Private Equity players, industry groups and investment management trade associations have initiated legal proceedings against the SEC, asserting that specific elements of the New Rules were outside of the SEC's authority and will unnecessarily increase the regulatory costs



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How Evalueserve is helping PE Firms and Advisers?

Evalueserve partners with private equity funds on every step of the fund lifecycle, including fund accounting, reporting, and valuation support to help managers focus on critical matters. Our expert research professionals currently work with leading private equity firms to create a significant impact on their investment process. We also work with portfolio companies for certain ad-hoc requirements helping them devise their growth strategies. We are partnering with our clients to assist them with the implementation of these rules and ensuring there are processes in place to facilitate compliance

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