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Final Rule — Private Fund Advisers and Documentation of Annual Compliance Review

October 2023

On August 23, 2023, the U.S. Securities and Exchange Commission ("**SEC**") adopted the Private Fund Advisers; Documentation of Registered Investment Adviser Compliance Reviews final rule (the "**Final Rule**"). According to the adopting release, these rules are designed to address several risks in the relationship between advisers with private funds and their investors, including a lack of transparency, conflicts of interest and lack of effective governance mechanisms for client disclosure, consent and oversight.

Scope and Impact of the Final Rule

The Final Rule adopts new rules and amendments under the U.S. Investment Advisers Act of 1940, as amended (the "**Advisers Act**") and it will require all private fund advisers, including certain exempt reporting advisers ("**ERAs**") to meet specific disclosure, consent and other requirements prior to engaging in certain "restricted" activities and granting certain preferential treatment to investors. The Final Rule will also require registered private fund advisers to (i) provide quarterly statements to investors with detailed fee, expense and performance information, (ii) perform annual financial statement audits of advised funds, and (iii) obtain a valuation or a fairness opinion in connection with adviser-led secondary transactions, among other requirements. Also, the Final Rule will require all registered private fund advisers to document annual compliance reviews in writing.

Private fund advisers are already scoping and assessing the potential impact of the Final Rule on their businesses and planning how to navigate the requirements of the Final Rule. Nuanced issues will surface, and market practice will evolve over the course of the next year, but the Final Rule will undoubtedly have a major impact on, and significantly increase compliance burdens for, private fund advisers. While the Final Rule will cause a significant shift in the regulatory landscape governing private fund advisers, these rules will not impact all private fund advisers equally (see "**Covered Firms**," "**Legacy Status**" and "**Compliance Deadlines**" below).

Covered Firms

As summarized in the table below, whether an adviser is subject to the Final Rule will generally depend on (i) the registration status of the adviser, (ii) whether the adviser is a U.S. or non-U.S. adviser and (iii) whether the adviser is managing a U.S. or non-U.S. private fund. In particular, some of the requirements of the Final Rule apply only to advisers registered or required to be registered under section 203 of the Investment Advisers Act of 1940 ("**RIAs**"), while others apply to all

private fund advisers (including ERAs, state-regulated advisers, advisers exempt from registration pursuant to foreign private adviser exemption and advisers that are otherwise unregistered with the SEC), subject to important exceptions noted below.

<table>
<tr><th>Rule</th><th>Advisers Subject to Rule</th><th>Exceptions</th></tr>
<tr><td>Quarterly Statement Rule</td><td>RIAs</td><td rowspan="5">None of these rules apply with respect to:
Non-U.S. advisers (registered or unregistered) with respect to their non-U.S. private funds (regardless of whether such funds have U.S. investors).
Advisers with respect to the securitized asset fund(s) they advise.
However, offshore advisers who have U.S.-based sub-advisers or managers integrated in their fund structure, or who manage master-feeder or parallel fund structures with a U.S. onshore fund, will have to consider scoping implications based on their specific situation. Additionally, in the Final Rule, the SEC indicated that a registered U.S. sub-adviser would not be exempted from compliance with the Quarterly Statement Rule with respect to a private fund whose primary adviser is not subject to the rule.
An RIA does not need to prepare a Quarterly Statement for a private fund that it advises if the private fund does not have at least two full fiscal quarters of operating results.</td></tr>
<tr><td>Audit Rule</td><td>RIAs</td></tr>
<tr><td>Adviser-Led Secondaries Rule</td><td>RIAs</td></tr>
<tr><td>Restricted Activities Rule</td><td>Private fund advisers</td></tr>
<tr><td>Preferential Treatment Rule</td><td>Private fund advisers</td></tr>
<tr><td>Written Compliance Review Rule</td><td>All registered advisers (whether they advise private funds or not)</td><td>Not applicable to unregistered advisers, onshore or offshore. Although there is ambiguity regarding application to registered offshore advisers to offshore funds, some firms are taking the position that registered offshore investment advisers advising only offshore funds would need to comply.</td></tr>
<tr><td>Anti-fraud Provisions of the Advisers Act; Fees for unperformed services and Liability waiver/Indemnification prohibitions</td><td>Private fund advisers</td><td>No exception (unless there is no U.S. jurisdictional nexus, or the activity is otherwise outside the scope of the Advisers Act).</td></tr>
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Compliance Deadlines and Transition Periods

The rules are effective November 13, 2023. As outlined in the table below, private fund advisers are subject to different compliance deadlines for the new rules.

Adviser Type	Compliance Dates
Smaller Private Fund Advisers (advisers with less than $1.5B in private fund assets under management)	Comply with all applicable rules (other than the Written Compliance Review Rule) **by March 14, 2025** (18 months after date of publication in the Federal Register, i.e., September 14, 2023).
Larger Private Fund Advisers (advisers with $1.5B or more in private fund assets under management)	Comply with the Adviser-Led Secondaries Rule, Restricted Activities Rule and Preferential Treatment Rule **by September 14, 2024** (12 months after date of publication in the Federal Register). Comply with the Quarterly Statement Rule and Audit Rule **by March 14, 2025** (18 months after date of publication in the Federal Register).
All Registered Investment Advisers	Document compliance reviews in writing per the Written Compliance Review Rule **starting on November 13, 2023** ● Whenever the adviser commences its review within the next 12 months after the compliance date, the review must be documented in writing. ● If an adviser has a review year that is partially complete by the compliance date and the adviser has already reviewed the adequacy of its policies and procedures in accordance with Rule 206(4)-7 for such period prior *to* the compliance date, the new documentation requirement will not apply retroactively to such period.

Legacy Status

The Final Rule allows for limited legacy status – exceptions for private funds in existence prior to compliance dates—for the prohibition aspects of (i) the Restricted Activities Rule that require investor consent (i.e., restrictions from borrowing from a private fund and from charging funds for certain investigation fees and expenses) and (ii) the Preferential Treatment Rule (i.e., redemption rights and information regarding portfolio holdings). As detailed below, private fund advisers must satisfy stringent, and in some cases unclear, conditions in order to achieve legacy status for existing contractual arrangements governing the funds that they manage.

Overview of Requirements and Practical Considerations

In the tables below we discuss the specific requirements of the Final Rule, and practical implications and questions that private fund advisers should consider.

Rules Generally Applicable to Private Fund Advisers (Regardless of Registration Status)

<table>
<tr><th colspan="2">Restricted Activities Rule</th></tr>
<tr><th>Final Rule Requirements</th><th>Practical Considerations</th></tr>
<tr><td> Investigation Fees. An adviser may not, directly or indirectly, charge or allocate to a private fund fees or expenses associated with an investigation of the adviser or its related persons by any governmental or regulatory authority, unless the investment adviser requests consent from each of the investors in such private fund and obtains written consent from at least a majority in interest of such investors that are not related persons of the adviser. Even with investor consent, the Restricted Activities Rule prohibits private fund advisers from charging or allocating to a private fund fees or expenses related to an investigation that results or has resulted in a court or governmental authority imposing a sanction for a violation of the Advisers Act or its related rules. </td><td> Required Actions: If seeking to charge investigation fees and expenses to a private fund client, request consent on a case-by-case basis from all private fund investors and obtain consent from at least a majority in interest of such investors.
Advisers should review and update their compliance policies and procedures as necessary to address this requirement. Legacy Status: Legacy status with respect to a private fund will apply only if the following criteria are met: the private fund has commenced operations[1] as of the compliance date,
the “governing agreements”[2] of the private fund were entered into in writing prior to the compliance date,[3] and
the prohibition would require the amendment of such governing agreements. Note: The legacy status provisions do not permit advisers to charge for fees or expenses related to an investigation that results or has resulted in a court or governmental authority imposing a sanction for a violation of the Act or the rules promulgated thereunder. Considerations and Questions: For advisers that do seek to charge investigation fees to private fund clients, the</td></tr>
</table>

[1] The commencement of operations includes any bona fide activity directed towards operating a private fund, including investment, fundraising, or operational activity (e.g., issuing capital calls, setting up a subscription facility for the fund, holding an initial fund closing, conducting due diligence on potential fund investments, and/or making an investment on behalf of the fund).

[2] The term “governing agreements” include contractual agreements that (i) govern the fund, which include, but are not limited to, the private fund’s operating or organizational agreements (e.g., the limited partnership agreement, the limited liability company agreement, articles of association, or by-laws), the subscription agreements, and side letters and (ii) govern the borrowing, loan, or extension of credit entered into by the private fund, which include, but are not limited to, the foregoing agreements from clause (i), if applicable, as well as promissory notes and credit agreements.

[3] The legacy provisions apply only with respect to advisers’ existing agreements with parties as of the compliance date. In the Adopting Release, the SEC notes that “an adviser may not add parties to a side letter after the compliance date in order to do indirectly what it is prohibited from doing directly.” However, the SEC also indicated that it would not view an adviser to a fund who admits new investors to an existing fund as violating the legacy provisions to the extent the applicable terms are set forth in the fund’s Limited partnership (or similar) agreement and applicable to all investors.

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	authority to charge investigation fees and expenses in a private fund's governing documents is necessary but not in and of itself sufficient for obtaining consent. ● In obtaining consents, advisers will generally be expected to list each category of fee or expense as a separate line item (as opposed to grouping fund expenses into broad categories) and describe how each such fee or expense is related to the relevant investigation. ● If an adviser has obtained consent pursuant to the Restricted Activities Rule, the adviser may charge a private fund client for fees and expenses associated with an investigation by the SEC of the adviser or its related persons for a potential violation of Section 206 of the Advisers Act; however, where an investigation results in a sanction for a violation of the Advisers Act, advisers that previously charged investigation fees and expenses to a private fund client will be required to refund those amounts (including attorneys' fees) to the relevant private fund client(s). ● The rule requires consent in writing, so negative consent will not be sufficient. ● The fund's governing documents may prescribe the manner and process for obtaining the applicable threshold of investor consent, and advisers need to keep records of consent obtained. ● Advisers must look-through affiliated entities to seek and obtain consent from unaffiliated investors. ● It is not clear whether an adviser would need to seek specific consent prior to charging or allocating to the fund fees or expenses associated with an investigation by foreign governmental authorities.
Examination and Compliance Fees. An adviser may not, directly or indirectly, charge or allocate to its private fund clients any regulatory or compliance fees or expenses, or fees or expenses associated with an examination, of the adviser or its related persons, unless the adviser distributes a written notice of any such fees or expenses, and the dollar amount thereof, to the investors of the private fund client within 45	**Required Actions**: ● If seeking to charge regulatory compliance or examination fees and expenses to a private fund client, provide written notice to investors within 45 days after the end of the relevant fiscal quarter in which the charge occurs (no need to obtain specific consent from investors). ● Advisers should review and consider updates to their expense allocation policies and

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days after the end of the fiscal quarter in which the charge occurs.	procedures to address this requirement. **Considerations and Questions**: ● Many advisers currently charge their private fund clients only for regulatory or compliance fees and expenses to the extent those expenses are specifically disclosed to clients. The difference between *compliance fees* and expenses related to an adviser's activities versus a private fund client's activities continues to be unclear, and the SEC has declined to draw a bright line. ● Importantly, the SEC did not prohibit charging regulatory/compliance fees and expenses to private funds as intended in the proposed rule, and the SEC noted that advisers and investors may continue to negotiate whether certain compliance, regulatory, or examination fees and expenses are charged to a fund, provided that the disclosure of such fees and expenses satisfies the requirements of the Final Rule. The SEC recognized that it did not want to disincentivize private fund advisers from using regulatory/compliance resources which benefit investors as long as they are disclosed. ● The SEC advised that the written notice should generally list each specific category of fee or expense as a separate line item with the dollar amount thereof, rather than group such fees and expenses into broad categories such as "compliance expenses." ● Advisers can include the written notice in their Quarterly Statement, which is also typically required to be delivered within 45 days of the end of the fiscal quarter.
Reducing Adviser Clawbacks for Taxes. An adviser may not, directly or indirectly, reduce the amount of an adviser clawback by actual, potential or hypothetical taxes applicable to the adviser, its related persons, or their respective owners or interest holders, unless the adviser distributes a written notice to the investors of the impacted private fund client setting forth the aggregate dollar amounts of the adviser clawback before and after any reduction of the clawback for actual, potential, or hypothetical taxes within 45 days after the end of the fiscal quarter in which the adviser clawback occurs.	**Required Actions**: ● For any after-tax clawback, provide written notice to investors within 45 days after the end of the fiscal quarter in which the clawback occurs setting out the aggregate dollar amounts of the clawback before and after the reduction. ● Advisers should review and update their compliance policies and procedures as appropriate to address this requirement. **Considerations and Questions**: ● The Final Rule does not prohibit the reduction of adviser clawbacks by actual, potential or hypothetical taxes and therefore the clawback provisions of fund documents will likely

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	remain unchanged following the rules taking effect (other than adding a requirement to send the relevant notice to investors if a clawback ever occurs). ● Registered advisers subject to the Quarterly Statement Rule may include the written notice in their Quarterly Statement which is also typically required to be delivered within 45 days of the end of the fiscal quarter.
Certain Non-Pro Rata Fee and Expense Allocations. An adviser may not, directly or indirectly, charge or allocate fees or expenses related to a portfolio investment (or a potential portfolio investment) on a non pro rata basis when multiple private funds and other clients advised by the adviser or its related persons have invested (or propose to invest) in the same portfolio investment, unless (i) the non-pro rata charge or allocation is fair and equitable under the circumstances and (ii) prior to charging or allocating such fees or expenses to a private fund client, the adviser distributes to each investor in the private fund a written notice of the non-pro rata charge or allocation and a description of how it is fair and equitable under the circumstances.	**Required Actions**: ● Deliver written notice to investors on a case-by-case basis before making non-pro rata expense allocations and charges to private fund clients. ● Advisers should review and update their compliance policies and procedures as appropriate to address this requirement. **Considerations and Questions**: ● The new rule places responsibility on the adviser for making a determination that the non pro rata allocation is fair and reasonable – and the SEC is likely to test the adviser's determination. The SEC stated that whether an allocation is fair and equitable will depend on factors relevant for the specific expense. The SEC provided the following as examples of factors that might be relevant: (i) whether the expense relates to a specific type of security that one private fund client holds, (ii) whether the expense relates to a bespoke structuring arrangement for one private fund client to participate in the portfolio investment, and (iii) whether one private fund client may receive a greater benefit from the expense relative to other private fund clients, such as the potential benefit of certain insurance policies. ● The SEC has not specified what "pro rata" means and therefore advisers will need to first decide how they interpret "pro rata" in respect of a particular transaction before being able to consider whether an expense is allocated pro rata. ● Delivering the specific notice to private fund investors on how the non-pro rata charge is fair and equitable before the adviser charges or allocates non-pro rata fees or expenses may be very difficult to do in practice. For example, it may be difficult to determine when a fee or expense is actually "charged" or "allocated" in practice (i.e., if an expense is funded through a subscription facility, is consent only required before a capital call is

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	issued to repay such facility). ● Advisers will need to consider implications on the logistics and timing of co-investment transactions, which are often executed on short timelines and frequently result in non-pro rata fee and expenses allocations (e.g., broken-deal charges).
Borrowing. An adviser may not, directly or indirectly, borrow money, securities, or other private fund assets, or receive a loan or an extension of credit from a private fund client, unless the adviser: (i) distributes to each investor in the private fund a written description of the material terms of, and requests each investor to consent to, such borrowing, loan, or extension of credit; and (ii) obtains written consent from at least a majority in interest of the private fund's investors that are not related persons of the adviser.	**Required Actions**: ● If seeking to borrow from a private fund client, deliver, on a case-by-case basis, to the private fund's investors a written description of material terms, request consent from all investors, and obtain consent from at least a majority in interest of private fund investors. ● Advisers will need to review and update their compliance policies and procedures to address this requirement. **Considerations and Questions**: ● The Final Rule does not enumerate specific terms that must be disclosed to investors in connection with an adviser's consent request, but rather only requires advisers disclose the material terms of the prospective borrowing. Such material terms may include, among others, the principal amount borrowed, the interest rate and the repayment schedule, depending on the facts and circumstances. ● The SEC clarified that it would not interpret ordinary course tax advances and management fee offsets as borrowings that are subject to the Final Rule. **Legacy Status**: Legacy status with respect to a private fund will apply only if the following criteria are met: ● the private fund has commenced operations as of the compliance date, ● the loan documentation of the private fund was entered into in writing prior to the compliance date, and ● the prohibitions would require the amendment of such loan documentation.

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Redemption Rights with Material Negative Effect. The Final Rule prohibits all private fund advisers from granting an investor in the private fund or a similar pool of assets the ability to redeem its interest on terms "that the adviser reasonably expects to have a material, negative effect on other investors" in that private fund or pool of assets. "Similar pool of assets" means a pooled investment vehicle (other than an investment company registered under the Investment Company Act of 1940, a company that elects to be regulated as such, or a securitized asset fund) with substantially similar investment policies, objectives, or strategies to those of the private fund managed by the investment adviser or its related persons. The SEC Noted that the scope of "similar pool of assets" is broader than the scope of the term "related portfolio" under the Marketing Rule. **Exceptions**: Private fund advisers are allowed to provide such preferential terms to investors in cases where (i) the ability to redeem is required by applicable laws, rules, regulations, or orders of any relevant foreign or U.S. government, state, or political subdivision to which the investor, private fund, or any similar pool of assets is subject, or (ii) the adviser offers the preferential redemption rights to all other existing investors and will continue to offer such redemption ability to all future investors in the same private fund or similar pool of assets, without qualification (e.g., no commitment size, affiliation requirements, or other limitations).	**Required Actions**: ● Refrain from providing preferential liquidity rights to investors (unless required by applicable law or regulation) or offer such rights to all current and future investors if the adviser reasonably expects such rights to have a material, negative effect on other investors. ● Advisers should review and update their compliance policies and procedures as appropriate to address this requirement. **Legacy Status**: Legacy status will apply only if the following criteria are met: ● the private fund has commenced operations as of the compliance date, ● the "governing agreements" of the private fund were entered into in writing prior to the compliance date, and ● the prohibition would require the amendment of such governing agreements. **Considerations and Questions**: ● The prohibition applies if the adviser reasonably expects the different redemption/withdrawal terms to have a material, negative effect on other investors. This puts the responsibility on advisers to make this determination, and the SEC will likely test the adviser's determinations. "Material negative effect on other investors" is not precisely defined in the Final Rule. Determinations in this respect may hinge on the specific rights being granted, the liquidity profile of the fund and its investment strategy. ● While the new restrictions on redemption rights will have a greater effect on open-ended funds, the rules also affect closed-ended funds because the rule captures an investor's preferential right to withdraw from a private fund (which many investors negotiate as part of side letter negotiations to deal with legal, regulatory, tax or other policy considerations). ● The carve-out for preferential redemption/withdrawal rights required by law or regulation does not extend to those required by an investor's individual policies, and any such redemption/withdrawal rights, if granted, must be offered to all other current and future

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	investors in the relevant private fund or similar pool without qualification. ● The SEC indicated that the term "similar pool of assets" is to be construed broadly. Feeders to the same master fund, parallel fund structures, alternative investment vehicles, co-investment vehicles, side cars and any other vehicles within a single fund structure will likely constitute "similar pools of assets" for these purposes. ● The SEC stated that whether a pool of assets managed by the adviser is "similar" to a private fund requires a facts and circumstances analysis, but a pool of assets with a materially different target return or sector focus, for example, would likely not have substantially similar investment policies, objectives, or strategies to those of the subject private fund. ● The SEC also noted that, under most (but not all) circumstances, a separately managed account would not be considered a similar pool of assets to a private fund. ● The SEC indicated that favorable liquidity terms provided through the private fund's governing documents (i.e., by a private fund offering different share classes, some with more favorable liquidity terms than others) presents the same concerns that the Final Rule seeks to address. For example, if an adviser offers a private fund with three share classes, each having different liquidity options but that are otherwise subject to the same terms (Class A, Class B, and Class C), the adviser likely cannot restrict Class A to, e.g., friends and family investors, legacy investors or those with a certain minimum commitment if the adviser reasonably expects there to be a material negative effect on other investors.
Information Rights with Material Negative Effect. The Final Rule prohibits advisers from providing preferential information rights about portfolio holdings or exposures of a private fund client (or of a similar pool of assets) to investors in such private fund where the adviser reasonably expects that providing the information would have a material, negative effect on other investors in such private fund (or similar pool of assets), except where such preferential information is offered	**Required Actions**: ● Refrain from providing preferential information rights about portfolio holdings or exposures to investors or offer such rights to all investors if the adviser reasonably expects such rights to have a material, negative effect on other investors. ● Advisers should review and update their compliance policies and procedures as appropriate to address this requirement.

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to all other existing investors in such private fund or similar pool of assets at the same time or substantially the same time.	**Legacy Status**: Legacy status will apply only if the following criteria are met: ● the private fund has commenced operations as of the compliance date, ● the "governing agreements" of the private fund were entered into in writing prior to the compliance date, and ● the prohibition would require the amendment of such governing agreements. **Considerations and Questions**: ● The prohibition applies if the adviser reasonably expects the different information rights to have a material, negative effect on other investors. This puts the responsibility on advisers to make this determination, and the SEC will likely test the adviser's determinations. "Material negative effect on other investors" is not precisely defined in the Final Rule. Determinations in this respect may hinge on the specific information disclosed and the liquidity profile of the fund and its investment strategy. Also, advisers will need to consider whether the information provided in the communication would have a material, negative effect on other investors in similar pools of assets. ● The SEC acknowledged that the ability to redeem is an important part of determining whether providing information would have a material, negative effect on other investors, and thus the SEC generally does not view preferential information rights provided to one or more investors in an illiquid private fund as having a material, negative effect on other investors. With that said, the SEC declined to provide a blanket exception for closed-ended funds, which may provide redemption/withdrawal rights under extraordinary circumstances. The SEC also noted that there may be cases where preferential information may be reasonably expected to have a material, negative effect on other investors in a private fund even when the preferred investor does not have the ability to redeem its interest in the private fund, and so whether preferential information violates the Final Rule requires a facts and circumstances analysis. ● There is no exception for preferential information that an investor is required to obtain under State or other law. Therefore, it is likely that any information advisers are required to provide to an investor by law or contract that the adviser reasonably expects would

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	have a material, negative effect on other investors, must be provided to all other investors at the same time or substantially the same time. With that said, the SEC acknowledged that the fee and expense transparency typically required by State law would generally not have a material, negative effect on other investors. ● In light of the Final Rule, advisers will need to be mindful about all communications between the adviser (including employees and personnel) and investors, including disclosures pursuant to rights granted via side letter, but also information conveyed in telephone conversations, email, due diligence questionnaires and any other mediums.
Any Preferential Rights. The Final Rule mandates that private fund advisers who provide *any* preferential treatment to any investor in a private fund provide: (i) *Advance written notice to prospective investors* in a private fund, prior to the investor's investment in such private fund, with specific information regarding *any preferential treatment* related to any *material economic terms* that the adviser or its related persons provide to other investors in the same private fund. (ii) *Written notice to current investors* in a private fund of *all preferential treatment* the adviser or its related persons has provided to other investors in the same private fund. This must be done: ● As soon as reasonably practicable following the investor's investment in a liquid private fund, and as soon as reasonably practicable following the end of the private fund's fundraising period for an illiquid fund. ● At least on an annual basis, with a written notice including specific information regarding any preferential treatment provided by the adviser or its related persons to other investors in the same private fund since the last	**Required Actions**: ● Provide advance written notice to prospective investors of any preferential treatment related to any material economic terms, provide written notice to current investors of all preferential treatment provided to other investors in the same private fund, and at least annually thereafter, provide written notice to current investors with specific information regarding any preferential treatment provided to other investors in that private fund since the last written notice provided. ● Advisers should review and update their compliance policies and procedures as appropriate to address this requirement. **Considerations and Questions**: ● The advance written notice requirements for prospective investors will only apply to preferential treatment related "to material economic terms," which the SEC describes as "those terms that a prospective investor would find most important and that would significantly impact its bargaining position," rather than to all preferential treatment. According to the release, the SEC would view the cost of investing, liquidity rights, fee breaks, and co-investment rights as material economic terms; however, the materiality standards are not defined in the Final Rule, leaving advisers to grapple with what constitutes "material economic terms" under the preferential treatment rule. ● The Final Rule requires an adviser to describe specifically the preferential treatment to convey its relevance (e.g., it is not sufficient to disclose that an investor received a preferential fee arrangement: the adviser must disclose the corresponding fee terms,

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written notice provided in accordance with the Final Rule (if any).	including the applicable rate or range of rates, and other contractual terms negotiated). Advisers may choose to make these disclosures by providing copies of side letters (with identifying information regarding other investors redacted) or, alternatively, providing a written summary of the preferential terms provided to other investors in the same private fund. ● The SEC staff stated that it is not prescribing a method of delivery, and mentions electronic delivery as an option (email, data room), subject to satisfying SEC guidance for electronic delivery. ● Advisers will need to distribute an annual notice if they agree to provide an investor with any preferential treatment since the last notice, but the SEC acknowledged, as a practical matter, a private fund that does not admit new investors or provide new terms to existing investors does not need to deliver an annual notice. However, an adviser that enters into a side letter after the closing date of the private fund must disclose any preferential terms in the side letter to all investors in the private fund. ● The disclosure requirement to prospective investors may change fund closing timing and logistics, and impact investor negotiations, while this aspect of the new rules may incentivize advisers to insist on “form” provisions given to all investors seeking a particular side letter right. ● There is no legacy status for this part of the Preferential Treatment Rule, which is likely to result in significant compliance and reporting obligations and costs for in-scope advisers’ existing private fund clients, including those that are closed and not admitting new investors. There is ambiguity in the Final Rule with regards to the potential application of the rule to closed-ended funds that have already closed. Given that this would entail a significant undertaking for certain sponsors, we anticipate that the market will generally oppose such application. ● Private fund advisers will need to consider the form of disclosures they want to provide and the pros and cons of different options (e.g., sending all side letters redacted or sending a summary).

Rules Applicable to Registered Private Fund Advisers

Quarterly Statement	
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Content of Quarterly Statement. The Final Rule requires registered advisers to prepare a quarterly statement ("**Quarterly Statement**") for each private fund they advise with information about the applicable fund's performance and any fees, expenses, and compensation allocated or paid to the adviser by such fund or by such fund's covered portfolio investments, each on a table with separate line items for each category of allocation or payment, reflecting the total dollar amount, presented both before and after the application of any offsets, rebates, or waivers. The Quarterly Statement must include "clear and prominent disclosures" regarding how all (i) expenses, (ii) payments, (iii) allocations, (iv) rebates, (v) waivers, and (vi) offsets are calculated with cross-references to the applicable methodology as provided in the fund's organizational and offering documents. The Quarterly Statement must be made in plain English and be easy to compare from one Quarterly Statement to the next. The standardized performance information to be included in the Quarterly Statement varies depending on whether a private fund client is liquid or illiquid. An "Illiquid fund" is a private fund that: (i) is not required to redeem interests upon an investor's request; and (ii) has limited opportunities, if any, for investors to withdraw before termination of the fund. A "Liquid fund" is a private fund that is not an illiquid fund. Private funds that fall into the "liquid fund" definition generally allow periodic investor redemptions, such	**Required Actions**: Advisers will need to: ● Review and update their compliance policies and procedures as appropriate to address this requirement. ● Identify relevant reporting dates and integrate into compliance checklists, design a process to obtain extensive data with respect to funds and portfolio-investments, including in the case of funds of funds, where obtaining such information will be a more significant undertaking. ● Determine whether its private fund client is an *illiquid or liquid* fund for purposes of the performance requirement, no later than the time the adviser sends the initial Quarterly Statement. The Final Rule adjusts the definition of an illiquid fund to focus on limitations to an investor's ability to redeem or withdraw. For example, most private equity and venture capital funds will likely fall under the illiquid fund definition, and most traditional hedge funds likely fall into the liquid bucket. ● Assess which reports to consolidate depending on each fund's structure, and determine which are the related funds that should be considered "similar pools of assets" for purposes of consolidation, given that the Final Rule takes a principles-based approach with regards to consolidated reporting. ● Create a customized tables with granular line items, including (i) a fund-level table for each private fund generally covering: fees, expenses; and compensation, as well as fund performance information, and (ii) a separate portfolio investment-level table for each covered portfolio investment providing: a detailed accounting of all portfolio investment compensation allocated or paid to the investment adviser or any of its related persons (as defined on Form ADV) by the covered portfolio investment during the reporting period, with separate line items for each category of allocation or payment (the portfolio-level disclosures are not limited to circumstances in which the adviser has discretion or

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<tr><td>as monthly, quarterly, or semi-annually.
● For a liquid fund, the adviser must include (i) annual net total returns for each fiscal year since inception or for the 10 years prior to the Quarterly Statement (whichever is shorter), (ii) the average annual net total returns shown over one, five, and 10 fiscal-year periods (as applicable); and (iii) the cumulative net total return for the current fiscal year (as of the most recent quarter covered by the Quarterly Statement)
● For an illiquid fund the adviser must provide, computed with and without the impact of any fund level subscription facilities: (i) gross and net IRR and MOIC for the illiquid fund and gross and net IRR and MOIC for the realized and unrealized portions of the illiquid fund's portfolio since inception; and (ii) a statement of contributions and distributions.
The Final Rule defines "statement of contributions and distributions" to mean a document that presents (i) all capital inflows the private fund has received from investors and all capital outflows the private fund has distributed to investors since the private fund's inception, with the value and date of each inflow and outflow; and (ii) the net asset value of the private fund as of the end of the reporting period.
Advisers must distribute the Quarterly Statement to that private fund's investors according to the corresponding timetable. For a private fund that is not a "fund of funds," the Quarterly Statement must be distributed to investors within 45 days of Q1, Q2, and Q3, and within 90 days of the end of the fiscal year. For fund of funds, the Quarterly Statement must be distributed within 75 days after the end of Q1, Q2, and Q3,</td><td>control over the portfolio investment).
● Calculate performance gross and net of subscription line financing.
● Revise disclosures to ensure they are in "plain English" – disclosures provided in marketing materials are often drafted with a sophisticated audience in mind.
● Consider required amendments to fund documents, e.g., to include cross-references to the Quarterly Statement.
Considerations and Questions:
● The Quarterly Statement requirement is a significant undertaking both for hedge fund and private equity advisers, especially those with multiple funds. It mandates an entirely new regulatory reporting form that advisers will have to distribute quarterly for every fund.
● There is considerable uncertainty as to the form that the required disclosures will take, and advisers will need to decide how to tailor the disclosures to the specific funds. The SEC specifically noted that specific reporting formats could be appropriate for certain types of funds but inappropriate for others given the nature of fees and expenses applicable to the type of fund, and noted that formatting that would be effective for a private equity buyout fund, could be misleading or confusing when applied to a private credit fund, a real estate fund or a hedge fund.
● Advisers are required to disclose information regarding only covered portfolio investments, defined as portfolio investments that allocated or paid the investment adviser or its related persons portfolio investment compensation during the reporting period.
● Advisers will need to determine how to specify different fees and expenses allocated to the funds (e.g., regulatory advice, fund formation, filings related to the offering) and reconcile quarterly statement disclosures with expense classifications and enumerations disclosed in private placement memoranda and limited partnership agreements in anticipation of increased investor and regulatory scrutiny of expenses.
● Due to interaction with the Preferential Treatment Rule, if including certain information in certain quarterly statements and not others (e.g., to provide statements tailored to specific investor's requests, as is technically allowed), advisers will have to assess the</td></tr>
</table>

Quarterly Statement	
Final Rule Requirements	**Practical Considerations**
and within 120 days after the end of the fiscal year. The Quarterly Statement must include the date through which the information is current and contain "prominent disclosure" of the criteria and assumptions used in calculating the performance. To the extent doing so would provide more meaningful information to the private fund's investors and would not be misleading, advisers must consolidate reporting for similar pools of assets.	type of information provided and whether it must be provided to all other investors. ● Advisers will have to assess interaction with marketing materials and also with the SEC's Marketing Rule in cases where the Quarterly Statement meets the definition of an "advertisement" (e.g., when it includes offers of new advisory services to existing investors or when it is distributed to prospective investors).

Adviser-Led Secondaries	
Final Rule Requirements	**Practical Considerations**
Valuation/Fairness Opinions and Summary of Material Business Relationships. The Final Rule would only allow an adviser conducting an adviser-led secondary transaction with respect to any private fund it advises to complete the transaction after it obtains and distributes to investors a written opinion from an independent opinion provider stating either (i) that the price being offered to the private fund for any assets being sold as part of the adviser-led secondary transaction is fair, or (ii) the value of any assets being sold as part of the adviser-led secondary transaction (either as a single amount or as a range). Advisers must also prepare and distribute a written summary to investors of any material business relationships the adviser or any of its related persons has or has had with the independent opinion provider within the two-year period immediately prior to the issuance of the fairness	**Required Actions**: ● Advisers should review and update their compliance policies and procedures as appropriate to address these requirements. **Considerations and Questions**: ● Obtaining either a fairness or valuation opinion is common market practice – the rule codifies this practice and adds specific requirements (e.g., summary of material relationships) and specific timing (prior to the due date of the election form). ● The new reporting requirements targeted to investors in private funds will have to be completed on a transaction-by-transaction basis. This differs from the adviser-led secondary requirements of the recently amended Form PF, which requires private equity fund advisers to submit a confidential report to the SEC with certain information within 60 days of the end of the quarter in which the adviser-led secondary transaction closes. ● The following transactions generally will not meet the definition of an adviser-led secondary transaction and generally will not require a fairness or valuation opinion: (i)

opinion or valuation opinion. Both the opinion and summary of material business relationships need to be distributed to investors prior to the due date of the election form for the adviser-led secondary transaction.	rebalancing between parallel funds; (ii) "season and sell" transactions; and (iii) most tender offers. ● Advisers will need to consider implications on the logistics and timing of adviser-led secondary transactions. ● The SEC did not provide specific requirements for fairness or valuation opinions, but it noted that these should be done in line with market practices and methodologies. The Adopting Release provides a non-exhaustive list of methodologies commonly used in creating these opinions including discounted cash flow, similar transactions, similar companies, and other comparable analysis. ● Fairness and valuation opinions and the summary of material business relationships can be distributed to investors through a data room subject to separate SEC guidance on the use of electronic delivery.

Audit Rule	
Final Rule Requirements	**Practical Considerations**
Private Fund Audit Requirement. The Final Rule requires registered private fund advisers to cause (or, if the adviser is not in a control relationship with the fund, to take all reasonable steps to cause) each private fund they advise directly or indirectly to undergo a financial statement audit that complies with the requirements of the audit provision of Rule 206(4)-2) under the Adviser's Act (the "**Custody Rule**"). The Final Rule requires a fund's audited financial statements to be distributed to current investors within 120 days of the end of the private fund's fiscal year, as currently required under the custody rule. For fund of funds, the time period is 180 days.	**Required Actions**: ● Advisers will need to update their custody rule compliance policies and procedures to reflect this requirement. **Considerations and Questions**: ● Unlike the Custody Rule regime, the Final Rule does not provide for the option of a surprise examination in lieu of an audit, sometimes a preferred option for smaller funds and SPVs treated as clients. This may cause certain advisers to reassess whether certain single-investment funds or funds-of-one would benefit from being recategorized as a separately managed account, to preserve the ability to rely on the surprise examination alternative. ● In the case of a fund that the adviser does not control and that is neither controlled by nor under common control with the adviser (e.g., where an adviser to a fund of funds selects an unaffiliated sub-adviser to implement a portion of the investment strategy), the adviser will need to take all reasonable steps to cause the fund to undergo an audit that meets the elements of the Private Fund Audit Requirement.

Written Compliance Review Rule	
Final Rule Requirements	**Practical Considerations**
Written Documentation of Annual Compliance Review. The Final Rule requires all registered advisers to document in writing the required annual review of their compliance policies and procedures, and the effectiveness of their implementation.	**Required Actions**: ● Advisers will need to review and update their compliance policies and procedures to address this requirement. **Considerations and Questions**: ● The annual compliance review has always been a focus of SEC examinations, and the focus likely will only increase now that the requirement to document it in writing has been codified. Although many private fund advisers are already documenting their annual reviews in writing as a matter of best practice, all advisers should review their written compliance reviews to ensure they are accurate and robust, keeping in mind that the SEC will use the written record of such reviews to identify potential compliance program weaknesses. ● In adopting amendments to the Advisers Act compliance rule, the SEC did not prescribe a specific format for the written documentation, allowing advisers flexibility to record the results of the annual review in a manner that best fits their business and to use the review procedures that they have found most effective. ● The required written documentation of the annual review under the compliance rule is meant to be made available to the SEC and the SEC staff and therefore should promptly be produced upon request. The SEC has indicated that that while the “promptly” standard imposes no specific time limit, in many cases advisers would be required to furnish records immediately or within a few hours of request. ● The compliance date for this rule is November 13, 2023. According to the SEC, whenever an adviser commences its review within the next 12 months after the compliance date, the review must be documented in writing. To the extent an adviser has a review year that is partially complete by the compliance date and the adviser has already reviewed the adequacy of its policies and procedures in accordance with Rule 206(4)-7 for such period prior to the compliance date, the new documentation requirement will not apply retroactively to such period.

Recordkeeping Rule Amendments	
Final Rule Requirements	**Practical Considerations**
Required Books and Records Rule. The Final Rule amends the books and records rule under the Advisers Act to require advisers who are registered or required to be registered to retain books and records related to the quarterly statement rule, the audit rule, the adviser-led secondaries rule, the preferential treatment rule and the restricted activities rule.	**Required Actions**: ● Advisers will need to review and update their compliance policies and procedures and recordkeeping charts to address this requirement. **Considerations and Questions**: ● Advisers will need to retain specific books and records that support their compliance with the previously mentioned rules, with respect to current investors and, in certain cases, with respect to prospective investors (e.g., the advance notice for purposes of the Preferential Treatment Rule). ● For example, to comply with the quarterly statements rule, advisers must retain (i) a copy of any distributed Statement (as well as a record of each addressee to which it is sent and the date on which it was sent), (ii) all records of how expenses, payments, allocations, rebates, offsets, waivers, and performance were calculated; and (iii) books and records to substantiate how the adviser determined whether a private fund client is liquid or illiquid. ● In adopting amendments to the Advisers Act books and records rule, the SEC stated that the amendments will enable an examiner to verify more easily that a fund is in compliance with these rules and will facilitate the more timely detection and remediation of non-compliance. These requirements will also help facilitate the SEC's enforcement and examination capabilities by improving the SEC staff's ability to assess an adviser's compliance with the final rule.

Applicable to All Advisers with Nexus to the U.S.

Activities Inconsistent with the Antifraud Provisions of the Advisers Act	
Final Rule Requirements	**Practical Considerations**
Fees for Unperformed Services. The SEC indicated that an adviser charging fees for monitoring, servicing, consulting, or	**Considerations and Questions**: ● An adviser is not permitted to charge fees for services that it does not provide or does

other services to portfolio investments that the adviser does not provide or reasonably expect to provide is already inconsistent with the adviser's fiduciary duty. The SEC noted that it has brought charges against advisers in the past for such violations.	not reasonably expect to provide. For example, if an adviser expects to provide monitoring services to a portfolio investment, the adviser is not prohibited from charging for those services. However, to the extent that the adviser ultimately does not provide the monitoring services, the adviser will need to refund any prepaid amounts attributable to unperformed services.
Adviser Liability Waiver or Indemnification Prohibition. The SEC did not adopt the proposed prohibitions against advisers seeking reimbursement, indemnification, exculpation, or limitation of liability by a private fund or its investors for a breach of fiduciary duty, willful misfeasance, bad faith, *negligence*, or recklessness in providing services to the private fund. However, the SEC noted that "a breach of the Federal fiduciary duty may involve conduct that is intentional, reckless or negligent" and pointed to its existing 2019 IA Fiduciary Duty Interpretation, stating that the antifraud provisions of Section 206(2) of the Advisers Act "can be adequately pled with only a showing of negligence" (as opposed to claims arising under Section 206(1) of the Advisers Act, which require a showing of scienter). The SEC also provided certain additional examples of activities that would be inconsistent with the adviser's fiduciary duty including: ● **Waiving of Fiduciary Duties**. The SEC confirmed that advisers cannot waive their fiduciary duty under the Advisers Act and that contractual provisions waiving the adviser's Federal fiduciary duty without specifying that the client retains certain non-waivable rights would violate the antifraud provisions of the Advisers Act. The SEC also noted a Staff position that the antifraud provisions of the Advisers Act would be violated where an adviser enters into a limited partnership agreement stating that "the adviser to the private fund or its related person, which is the general partner of the fund, to the	**Considerations and Questions**: ● The SEC did not adopt the proposed ordinary negligence standard, nor did it outright prohibit a gross negligence standard, but it did raise ambiguities and uncertainties that private fund advisers are and will continue to consider over the coming period (e.g., whether seeking reimbursement or otherwise limiting adviser liability for negligence in providing advisory services could, under certain circumstances, be inconsistent with the antifraud provisions of the Advisers Act).

maximum extent permitted by applicable law, will not be subject to any duties or standards (including fiduciary or similar duties or standards) existing under the Advisers Act or that the adviser can receive indemnification or exculpation for breaching its Federal fiduciary duty." ● **Reimbursement for Breach of Fiduciary Duty**. The SEC suggested that an adviser seeking reimbursement, indemnification, or exculpation for breaching its federal fiduciary duty would effectively be seeking a waiver of the adviser's fiduciary duty that would be invalid under the Advisers Act. ● **Ambiguous State Law Waivers**. The SEC did not take a position on fiduciary duties under state law, but it did suggest that where a state law waiver is ambiguous as to whether it is applicable to the Federal fiduciary duty, the SEC would interpret such a waiver as waiving the Federal fiduciary duty in violation of the antifraud provisions of the Advisers Act. We note that the SEC did acknowledge that the application of the fiduciary duty flows from the functions the adviser has agreed to take on for its client and can differ between retail and private fund clients. The SEC also reaffirmed that whether a hedge clause in an agreement with an institutional client violates the antifraud provisions of the Advisers Act involves a facts and circumstances determination.	

Conclusion

Many gray areas and nuanced issues have emerged and will continue to develop on the road to implementation. Private fund advisers are already planning and preparing for compliance with the new rules, with a careful eye on how market practice develops around implementation of these new rules. Given the significance of these new rules, private fund managers are starting to assess the impact for their business and planning now as these new rules will require significant lead time to implement from a business, operational, legal and compliance perspective.

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