

SEC Chair Gensler signals increased regulatory scrutiny for private fund managers

November 15, 2021 | Client Update | 3-minute read

Chair Gary Gensler signaled once again, and perhaps in the clearest terms to date, his intention to bring greater scrutiny to the private fund industry. During prepared remarks, Chair Gensler indicated that SEC staff are considering changes to practices regarding private fund fees and expenses, side letters, performance metrics, fiduciary duty and conflicts of interest, and Form PF.

On November 10, 2021, in prepared remarks at the Institutional Limited Partners Association Summit, Securities and Exchange Commission (SEC) Chair Gary Gensler signaled once again, and perhaps in the clearest terms to date, his intention to bring greater scrutiny to the private fund industry. His remarks are available [here](#).

Key takeaways:

- **Fees and expenses.** Gensler expressed concern about a perceived lack of transparency in private fund fees and expenses and singled out consulting fees, advisory fees, monitoring fees, servicing fees, transaction fees, and director's fees, among others, during his remarks. He noted that he has asked the SEC staff to consider potential recommendations to bring greater transparency to fee arrangements.
- **Side letters.** Gensler expressed concern about side letters, particularly where they create preferred liquidity terms or disclosures for certain investors. In his view, side letters can create an uneven playing field between investors. He noted that he has asked the SEC staff to consider recommendations regarding how the SEC can level that playing field and strengthen transparency or whether certain side letter provisions should be prohibited.
- **Performance metrics.** Gensler has asked the SEC staff to consider ways to improve the transparency for private fund performance metrics, particularly so that there can be a more meaningful comparison between public markets (e.g. mutual funds) and private funds. He suggested that basic facts about private funds are not readily available, including with respect to the fees they implement or their use of leverage, which currently makes these comparisons difficult.
- **Fiduciary duty and conflicts of interest.** Gensler has asked the SEC staff to consider how the SEC can better mitigate the effects of conflicts of interest between general partners, their affiliates, and investors. This could include possible prohibitions on certain conflicts and practices through rulemaking. Gensler also expressed concern about attempts to waive an adviser's fiduciary duty at the state or federal level (he noted specifically that the Institutional Limited Partners Association has data indicating that 48 percent of institutional investors reported that general partners had modified or reduced their fiduciary duties in new capital allocations). He emphasized to the audience that contract provisions purporting to waive an adviser's federal fiduciary duty are inconsistent with the Investment Advisers Act of 1940, regardless of the sophistication of the client.
- **Form PF.** With respect to Form PF, Gensler believes it is appropriate to consider whether more granular or timelier information would be useful, particularly in light of the fact that the role of private funds was not immediately apparent in March 2020 when the Treasury market experienced turmoil following the onset of the COVID-19 pandemic. He noted that he has asked the SEC staff for recommendations for the SEC's consideration to enhance reporting and

disclosure on Form PF or other reforms and that the SEC is working on this initiative with the CFTC, as well as FSOC, Treasury, and the Federal Reserve. We note that this initiative was disclosed on the SEC's Spring 2021 Regulatory Agenda, available [here](#).

While it is unclear what any of these proposals will ultimately look like, the overall tenor of the speech is a clear indication that private fund managers should expect increased scrutiny from the SEC, whether in the form of increased examinations, enforcement actions or new regulations.

If you have any questions regarding the matters covered in this publication, please reach out to any of the lawyers listed below or your usual Davis Polk contact.

Jennifer Grant Cooper

+1 212 450 4492
jennifer.cooper@davispolk.com

John G. Crowley

+1 212 450 4550
john.crowley@davispolk.com

Lee Hochbaum

+1 212 450 4736
lee.hochbaum@davispolk.com

Michael S. Hong

+1 212 450 4048
michael.hong@davispolk.com

Sarah E. Kim

+1 212 450 4408
sarah.e.kim@davispolk.com

Leor Landa

+1 212 450 6160
leor.landa@davispolk.com

Gregory S. Rowland

+1 212 450 4930
gregory.rowland@davispolk.com

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