



SEC Issues New Private Fund Rules:

Real Estate Fund Managers Should Note Additional Reporting and/or Compliance Requirements^{1,2}

In August 2023, the Securities and Exchange Commission adopted new rules and rule amendments to enhance the regulation of private fund advisers and update the existing compliance rule that applies to all investment advisers. *These new rules reflect the most substantial overhaul of private funds regulation since Dodd-Frank in 2010.*

Specifically, the new rules and amendments are designed to protect private fund investors by increasing transparency, competition and efficiency in the private funds market and will impact all investment advisers, including real estate investment managers.

The SEC adopted two new rules for all advisers: the “Restricted Activities Rule” and the “Preferential Treatment Rule”

The new rules that apply to all private fund advisers:

- **Restricted Activities Rule: Prohibits engaging in certain activities and practices that are contrary to the public interest and the protection of investors unless they provide certain disclosures to investors, and in some cases, receive investor consent.** This new Rule states that, unless disclosed, advisers may not: (1) charge investors for their regulatory or compliance fees or expenses; (2) claw-back taxes from the funds; or (3) allocate or charge portfolio-level fees or expenses on a non-pro-rata basis. And without consent from a majority in the interest of private funds investors

(excluding advisers’ and related persons’ interests), advisers may not charge their clients for fees or expenses associated with governmental or regulatory investigations. Also, without investor consent, advisers may not borrow assets from their private fund clients.

- **Preferential Treatment Rule: Prohibits providing certain types of preferential treatment that have a material negative effect on other investors and prohibits other types of preferential treatment unless disclosed to current and prospective investors.** The new rule generally prevents private fund advisers from allowing any investor to redeem its interests on terms reasonably expected to materially harm other investors, and also generally prohibits advisers from disclosing information to any investor that they reasonably expect would materially harm other investors. The new rule also

prohibits any other preferential treatment, unless such treatment is detailed in annual written disclosures.

For registered advisers, the SEC adopted three additional new rules: the “Quarterly Statement Rule,” the “Private Fund Audit Rule” and the “Adviser-led Secondaries Rule,” as well as amendments to the Advisers Act Compliance Rule

The new rules and compliance amendment that apply to private fund advisers registered with the SEC:

- **Quarterly Statement Rule: Provides investors with quarterly statements detailing information regarding private fund performance, fees and expenses.** This new rule requires registered advisers to make quarterly disclosures about fees, expenses, performance and potential conflicts of interest, unless quarterly disclosures complying with the Rule are already prepared by another party. The requisite quarterly statements must prominently disclose how expenses and fee offsets are calculated, as well as performance results calculated with and without capital call lines, with cross-references to funds’ governing documents. The SEC also amended Rule 204-2 to require advisers to retain books and records in connection with the preparation and distribution of these quarterly statements.
- **Private Fund Audit Rule: Requires an annual audit for each private fund.** Intended to prevent asset misappropriation and ensure accurate valuations, this new rule requires an annual independent financial statement audit for each registered adviser’s fund that complies with Rule 206(4)-2 (the Custody Rule requires advisers that have custody of client securities or funds to implement a set of controls designed to protect those client assets from being lost, misused, or misappropriated). But this new rule does not, as originally proposed, impose any audit requirements on top of those in the Custody Rule. Nor does it require auditors to report

any issues to the SEC.

- **Adviser-led Secondaries Rule: Requires a fairness opinion or valuation opinion in connection with an adviser-led secondary transaction.** Also intended to prevent fraud and ensure accurate valuations, this new rule requires either a fairness or a valuation opinion from an independent provider in connection with any secondary transaction led by a registered adviser.

Additionally, the amendments will require all registered advisers, including those that do not advise private funds, to document in writing their annual review of compliance policies and procedures.

Impact:

- For some real estate investment managers, the newly published rules will significantly increase their administrative requirements and, in certain cases, require the services of an independent third-party provider for services such as valuations, fairness opinions or financial statement audits.
- For many, additional reporting and/or compliance requirements will need to be met, increasing the time requirements of internal or third-party professionals.
- Compliance is required within 12-18 months, depending on the particular rule and the size of the adviser.

As with all new rules and rule amendments, there may be clarifications or alternative interpretations that impact the application of these rules to real estate advisers or advisers in general. We recommend that advisers consult with their legal representatives for up-to-date interpretation of these rules and amendments.

For questions or needs concerning any of the topics covered in this overview, please contact [Josh Herrenkohl](#), Senior Managing Director, or [Connie Tirondola](#), Managing Director, at FTI Consulting.

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This document is a high-level summary of selected content from the following two websites:

¹ Securities and Exchange Commission Rin 3235-AN07 summary - sec.gov. [Release of the Securities and Exchange Commission \(“SEC”\), Release No. IA-6383, File No. S7-03-22.](#) (2023, August 23).

² Fact Sheet Private Fund Adviser Reforms: Final Rules - sec.gov. [Fact Sheet: “Private Fund Adviser Reforms: Final Rules.”](#) (2023, August 23).

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