

Chair Gary Gensler
Securities and Exchange Commission
100 F St NE
Washington, DC 20549

February 21, 2023

Chair Gensler,

The following 29 undersigned organizations and individuals urge the Securities and Exchange Commission (“the Commission”) to finalize a strong set of its proposals that bring much needed transparency to the \$18 trillion in private funds and provide investors in those funds with a detailed breakdown about their investments that they are not able to currently obtain to make informed investment decisions.

As the Commission itself has found, the \$18 trillion in gross assets of private funds made up predominantly of hedge funds and private equity firms now is nearly the same size as the \$23 trillion in assets in the banking system.¹ However, unlike banks whose assets are subject to oversight by the Federal Reserve, Office of the Comptroller of the Currency (OCC), and Federal Deposit Insurance Corporation (FDIC), private funds have nowhere near the same level of reporting requirements to both regulators or their investors.

Despite the much lighter reporting requirements, policymakers still have been willing to backstop private fund losses with public funds once a decade starting from the bailout of hedge fund Long Term Capital Management in 1998, the Great Financial Crisis of 2008, and in March 2020.

The SEC’s expansion of Form PF is critical to ensuring policymakers and other regulators have the insight they need ahead of an economic downturn

The inherent lack of transparency in the \$18 trillion in private funds leaves policymakers in the dark as to the risks to the financial system in an economic downturn, leading Federal Reserve Chair Jerome Powell recently to state that private funds require structural changes.² The SEC has the authority to help provide policymakers with the adequate information they need to make informed policy decisions.

We are therefore calling for the Commission to follow through with its proposals and issue a final rule that among its other proposals:

¹ Board of Governors of the Federal Reserve System. Assets and Liabilities of Commercial Banks in the United States. [The Fed - Assets and Liabilities of Commercial Banks in the United States - H.8 - February 17, 2023 \(federalreserve.gov\)](https://www.federalreserve.gov/monetarypolicy/asset-liability/20230217)

² Campbell, Kyle. American Banker. Powell: Nonbanks need structural reforms, not Fed backstop. Jan 10, 2023. [Powell: Nonbanks need structural reforms, not Fed backstop | American Banker](https://www.americanbanker.com/news/powell-nonbanks-need-structural-reforms-not-fed-backstop)

- Requires private funds to disclose all of their individual investments, financing associated with them, and investments elsewhere in the capital structure
- Hedge fund disclosure of withdrawals or losses of 20% or more of their Net Asset Value
- Defaults by a fund's counterparty and material change in relationship with the fund's prime broker

Investors in private funds do not have the necessary information nor resources to properly evaluate their investments requiring the SEC to intervene

The Commission also has a critical role in improving the inefficient and dysfunctional way that investors currently negotiate investment terms in private funds, a process which often leaves them without the basic information necessary to evaluate their investments.

Such an antiquated process has unfairly allowed for the transfer of billions of dollars in wealth from public pensions, university endowments, foundations, and other institutional investors to the private fund advisers who have been able to exploit the current system's inefficiencies and opaqueness.

Some of the largest investors in private funds continue to be unable to receive basic information from their advisers including a breakdown of the fees and expenses they are being charged.³

Therefore the Commission uniquely is in a position to collectively ensure that investors in private funds are adequately receiving basic but important information such as:

- Detailed breakdowns of the fees and expenses charged to them
- How the returns on illiquid investments are being calculated
- Whether other investors have special arrangements with the private fund adviser via "side letters"

Similarly, the Commission has the authority under the Investment Advisers Act of 1940 to restrict certain fees from improperly being charged⁴ such as the highly questionable practice of collecting accelerated monitoring fees from portfolio companies when no actual service is being provided. The pro-rated division of those supposed fees among multiple private fund advisers also suggests that these are in fact backdoor dividends that are using a loophole to avoid paying taxes.⁵

³ Willmer, Sabrina. Bloomberg News. Private Equity's Opaque Costs Mystify the Pensions That Pay Them. Mar 29, 2022. <https://www.bloomberg.com/news/articles/2022-03-29/private-equity-firm-fees-create-headache-for-pensi-on-plans>

⁴ Baker Hostetler. The SEC Continues Its Regulatory Focus on Advisory Fees and Expenses. May 2, 2018. <https://www.bakerlaw.com/alerts/the-sec-continues-its-regulatory-focus-on-advisory-fees-and-expenses>

⁵ Polsky, Gregg D. University Georgia School of Law. Private Equity Monitoring Fees as Disguised Dividends: Collateral Impact. Jul 4, 2014. https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2461733

Conclusion

The \$18 trillion private fund industry has been able to operate on a special set of rules and rely on outdated exemptions for decades, and it is therefore imperative that the SEC finalize rules consistent with its proposals to ensure that policymakers and other regulatory agencies have adequate information about the holdings and risks in private funds to properly safeguard the financial system and economy.

Similarly, given the thousands of different investors that now invest in private funds, many of whom are investing public money, private fund advisers must be subjected to a minimum set of disclosures on the fees, returns, and other special arrangements being made so that those investors have the information they need.

Sincerely,

Americans for Financial Reform Education Fund

AFL-CIO

American Federation of State, County, and Municipal Employees

American Economic Liberties Project

American Federation of Teachers

Bargaining for the Common Good

Better Markets

Center for Economic Policy Research

Communications Workers of America

Consumer Action

Consumer Federation of America

Economic Policy Institute

Good Jobs First

Inquilinxs Unidxs por Justicia

Institute for Agriculture and Trade Policy

Interfaith Center on Corporate Responsibility

Laura Katz Olson

National Education Association

National Employment Law Project

Revolving Door Project

Public Citizen

SOC Investment Group

Strong For All Coalition

Sunrise Project

Texas Campaign for the Environment

Transparency Task Force

UNITE HERE Local 11

United for Respect

20/20 Vision

cc: Commissioner Caroline A. Crenshaw

Commissioner Jaime Lizárraga

Commissioner Mark T. Uyeda

Commissioner Hester M. Peirce