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April 25, 2022

Ms. Vanessa A. Countryman
Secretary
U.S. Securities and Exchange Commission
100 F. Street NE
Washington, DC 20549-1090

Submitted via email to rules-comments@sec.gov

Re: SEC File Number S7-03-22 (SEC Release No. IA-5955)

Dear Ms. Countryman:

I am the Chief Executive Officer of the Regulatory Fundamentals Group LLC ("RFG"), a consulting firm that represents a consortium of 25 leading nonprofit investment offices with over $200 billion in investable assets combined. These institutional allocators are sophisticated investors serving non-profit missions. Charged with investing billions of dollars in diverse pools of assets, each is subject to fiduciary standards of care which are derived from applicable state and federal laws and from their own internal and external investment mandates. RFG's members invest in the types of private funds whose investment advisers would be impacted by the Private Fund Proposal (as defined below). These private fund investments are an important component of our clients' investment programs, and their capital is an important part of the private capital ecosystem. Our clients seek to preserve open access to these markets.

RFG submits this letter in response to the request of the Securities and Exchange Commission (the "Commission") for comments in connection with Investment Advisers Act Release No. 5955, which proposes new rules under and amendments to the Investment Advisers Act of 1940, as amended (the "Advisers Act"), that would expand the regulatory framework under which private fund advisers operate (the "Private Fund Proposal"). This letter is based on active discussion with RFG's members but does not necessarily reflect the position of any specific member.

RFG had previously written to the SEC requesting an extension of the comment period in order to provide sufficient time to evaluate the significant impact the Private Fund Proposal is likely to have on the entire private fund industry-- resulting from both (i) any newly adopted requirements for advisers and (ii) the internal operational changes such requirements will

impose on limited partners. We felt that a thoughtful review, which might even have the benefit of reflecting an industry-wide dialogue, would help us to better inform the Commission's decision-making process.

Since the comment period has not been extended, RFG is sharing its initial thoughts on the aspects of the proposal that it believes will have the greatest impact on non-profit institutional investors. In the proposal, the staff asked numerous important and insightful questions; however, given time constraints, RFG is unable to provide comments on anything other than a few of the specific proposals and, even with respect to those few proposals, our comments are at a high level.

Specifically, we view the following aspects of the Private Fund Proposal to be the most important to the non-profit institutional investors RFG represents:

- prohibition on preferential transparency;
- prohibition on preferential liquidity;
- standard of care and fiduciary duty;
- MFN and disclosure of preferential rights;
- Quarterly reporting requirements;
- tax-netting in clawbacks;
- adviser-led secondaries;
- prohibitions on borrowing from a fund; and
- the unintended consequences the rule might impose on new advisers and investors.

These preliminary concerns are addressed in more detail below.

1. **Proposed Rule 211(h)(2)-3(a)(2) – Prohibition on Preferential Transparency**

Though well-intentioned, we do not support the currently proposed limitations on granting preferential transparency. We recognize that the Commission has attempted to set a standard that would permit advisers to be transparent with investors so long as such transparency does not materially harm other investors in the private fund or in a substantially similar pool of assets. However, "material harm" and "substantially similar" are vague and potentially broad concepts. RFG is concerned that, given the potential consequences of a rule violation, advisers will be strongly incentivized to be overly conservative in deciding what they can disclose to investors. This could discourage an adviser from providing information it would otherwise share with an investor out of concern that providing the information could be alleged to have a material, negative effect on other investors. Thus, the rule will likely cause investors that currently receive enhanced transparency rights for a particular fund to receive less transparency, rather than increasing transparency across the board for all investors. We describe below how this will negatively impact all investors.

Rather than limiting the freedom of investors and advisers to negotiate transparency rights, we strongly endorse a requirement for advisers to fully disclose, on an anonymized basis, a summary of the transparency terms they have granted.[1] Armed with this information, new investors will be able to make informed decisions as to whether and on what terms they will invest in a given private fund. Such disclosure would provide each investor with information it needs to evaluate the investment and to negotiate for the transparency rights that work for its needs.

In contrast with the freedom to contract enhanced by a disclosure requirement, any reduction of transparency triggered by the current proposal will materially weaken the ability of investors as a whole to oversee an adviser's performance, both from an investment and risk management perspective. Providing enhanced transparency rights to some investors not only helps those investors to better vet and monitor an adviser's performance and adherence to its investment mandate, but frequently benefits all investors because of their alignment in the commonly-held portfolios. The investor that receives better transparency will often use that information to offer feedback to an adviser and impose additional accountability. Reducing transparency overall by eliminating preferential transparency translates into fewer opportunities for a manager to be challenged or questioned. It would be a perverse regulatory outcome to diminish what enhanced opportunities are granted by a manager to at least some investors to engage on important issues, which generally redound to the benefit of all investors.

Also, advisers have increasingly used limited partner advisory committees to serve as a sounding board and mechanism for additional accountability. Members of those committees clearly need access to information to serve that function meaningfully. It is not clear to us whether the proposal is intended to curtail non-written forms of differential transparency.

We are especially concerned that the proposed limitations would hamper, or change the nature of, the live discussions investors currently are allowed to have with their advisers. Similar to the detrimental effects of reduced written transparency, if an adviser can hide behind the pretext of not being permitted to discuss the portfolio with an investor because of the proposed rule, investors as a whole will have a diminished ability to evaluate whether the adviser is being a good steward of the funds it is managing and whether the adviser remains worthy of trust. As a result, investors will lose that additional opportunity to hold the adviser accountable to its investors.

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[1] Disclosure of the terms of side letters negotiated before the rule is adopted may require the renegotiation of those side letters and could therefore impose significant legal and other out-of-pocket costs and administrative burdens on both advisers and limited partners. For this reason, we would not require disclosure of the terms negotiated before the rule is adopted by private equity and other closed end funds. In this situation, given the closed nature of the fund, an increase in costs would not serve a useful purpose, as it will not assist a new partner seeking to make an investment decision. We do support disclosure of summary hedge fund side letter terms on an anonymized basis, as the utility of such disclosure for new investors in open-ended funds outweighs the costs of renegotiating such arrangements that will be borne by industry participants.

Moreover, advisers are wary of non-confidential treatment of their proprietary information, and generally seek to limit the number of parties who have access to such information. It makes sense, therefore, that preferential transparency is granted to those investors that an adviser has a relationship with and trusts most. Since many funds are oversubscribed, if an investor with whom an adviser has an existing relationship requests enhanced transparency in the next fund being raised by the adviser, an adviser may either (i) choose not to admit the requesting investor or (ii) choose not to admit those investors that do not have an established relationship with the adviser, in each case in an attempt to avoid providing transparency to a party the adviser is not yet comfortable sharing information with. The latter election by an adviser would most likely hurt smaller or less established investors seeking access to specific funds or investors with unique needs (such as freedom of information act requirements).

While the Commission notes it is concerned that preferential transparency rights are used by some investors to front-run other investors, most fund operating documents already control for front-running as part of customary confidentiality provisions by restricting the use of fund information by investors for reasons other than monitoring fund investments. In addition, preferential transparency is almost always given on a lagged basis, further minimizing the risk of harm to other investors. Advisers have every incentive to police these provisions vigorously. In addition, we believe that the vast majority of investors that benefit from enhanced transparency rights use the rights solely for the legitimate purpose of improving their own diligence, risk and portfolio management functions, and in all but tail scenarios that involve bad actors, such rights have no negative impact on fellow investors. If anything, allowing enhanced transparency rights for some investors results in enhanced vetting and monitoring of advisers to commingled funds and benefits all investors in such funds. In short, the potential for problematic front-running (if it exists) is not so great and the enforcement by industry participants is not so lacking that rulemaking in this area is needed, particularly when the proposed solution could significantly curtail legitimate and long-standing practices that benefit all investors.

To re-emphasize our concerns, we believe that the proposed rule as currently drafted would likely lead to less, rather than more, transparency in the funds industry overall. In addition to directly harming the investors that would stand to lose enhanced transparency rights as a result of the rule, all investors would lose the benefits they currently derive from such shared rights and some may lose access to investing in certain funds altogether -- all this would occur without a clearly identifiable and significant offsetting benefit. This result is especially problematic since the Commission's underlying concerns can be addressed through increased disclosure.

Finally, we urge that any adopted proposal should not retroactively modify existing transparency rights. Investors have typically traded off other legal and economic rights as part of the process of obtaining enhanced transparency. For example, an investor may have agreed to receive less favorable fee terms in order to secure enhanced transparency rights. Retroactively stripping investors of the information rights they actively negotiated for will leave those investors empty-handed, while simultaneously creating a windfall to the advisers who will be allowed to keep the benefit of the bargain they struck when negotiating these terms. If the

rules are applied on a prospective basis only, all industry participants will have the opportunity to negotiate from the same starting point. To be clear, we are not suggesting that passing the proposed rule while preserving existing arrangements would be a good compromise for investors: we are simply noting that passing the rule without exempting existing arrangements would make a bad outcome for the industry even worse.

2. **Proposed Rule 211(h)(2)-3(a)(1) – Limitation on Preferential Liquidity**

Consistent with our support for comprehensive disclosure of preferential transparency on an anonymized basis, we support clear, upfront, and ongoing disclosure of a summary of alternative liquidity arrangements on an anonymized basis. We do not, however, support the proposed limitations on preferential liquidity, at least not in the form proposed by the Commission. Here again we are concerned that the vague standards applied may cause an adviser to make self-protective decisions. We discuss below, in more detail, why we do not support the proposed limitations on preferential liquidity.

Different liquidity options allow investors to build balanced portfolios and negotiate reduced fees. Institutional investors have invested in liquid and illiquid assets to meet the near- and long-term needs of their respective missions. This flexibility allows investors to take advantage of an adviser's need for stable capital to hire staff, build compliance systems and allow certain investment ideas to fully mature. Those investors that can leave their assets invested in a fund for a longer period may prefer to "trade" access to liquidity for lower fees or for other favorable economic terms, which is especially important to long-term investors that are seeking to reduce the fee burden for their institutions. Indeed, funds frequently offer separate classes of interest which allow investors to elect greater or lesser liquidity in return for higher or lower fees, respectively. The proposed rule could potentially stop advisers from offering such commonly utilized terms due to concerns with regulatory violations.

Conversely, some investors require special redemption rights in specific circumstances (including non-discretionary legal and regulatory circumstances, such as in connection with ERISA). This prohibition, should it be adopted, may mean that such investors will no longer be able to access private fund investments altogether, which historically have been important drivers of returns for many investors. Additionally, the Private Fund Proposal fails to clearly address how or whether this prohibition will impact an adviser's ability to cause mandatory investor withdrawal in certain circumstances, including for regulatory reasons. If such discretion was limited, an adviser would have limited ability to mitigate certain regulatory issues, which could very well have an adverse effect on the other fund investors.

As there is no objective standard for what constitutes "preferential" liquidity, we are concerned that the proposed rule will be difficult to interpret and enforce as a practical matter. For instance, is monthly liquidity with a three-year initial lockup and a 30-day notice period "better" than semi-annual liquidity with a one-year initial lockup and a 45-day notice period? The answer depends on the specific applicable facts and circumstances, including the particular

goals of a given investor, the characteristics of the fund's underlying portfolio, and the other elements of the entire package of terms at issue, including fees and transparency rights, just to name a few.

If the limitations on preferential liquidity are to be adopted, we think it is critical for the Commission to provide more guidance for advisers and investors alike on what the applicable standard means and how it should be applied. Absent specific guidance, we fear that many advisers of liquid funds will take a "conservative" position as to what the regulation means and only offer a single liquidity option. While we would prefer that this proposed rule be removed in its entirety, if it is enacted we suggest the following modification: In concert with the concept of full, anonymized disclosure of a summary of all liquidity terms an adviser is willing to give,[2] we propose that if a given package of liquidity terms is deemed preferential to another set of terms, it should be permissible for the adviser to offer both sets of terms as long as such terms are available to all investors who wish to elect them. Setting a one-size fits all liquidity profile for each fund would have the perverse effect of causing many advisers, especially the larger more established ones, to offer less flexibility with respect to liquidity to the detriment of investors. Thus, it would limit overall investment options available to investors.

The ability to offer different liquidity thresholds supports the goals of prudent fund management and competitive markets. Different liquidity options are an important component of portfolio construction, especially for new advisers. Many are willing to provide attractive liquidity (or other terms) to obtain the operating capital and initial fund investment often provided by "seed investors." More generally, it is common for advisers to offer different and favorable liquidity terms as a way to attract early investment, strategic, or large commitment investors into newly launched funds. These arrangements encourage new advisers, increase competition for capital and create a more diverse group of advisers. Some studies suggest that "new" advisers often generate outsized returns[3], fund under-resourced areas and fuel innovation. Indeed, many of our members have significant portions of their portfolio reserved for allocation to emerging advisers for these reasons. To force lock-step liquidity across the market will limit the ability of new advisers to attract initial capital.

Finally, "seed" investments are particularly important as the industry seeks to encourage a new, more diverse group of advisers to enter the market. Many of these new advisers may seek to establish their own firms, rather than grow through the ranks of large, entrenched organizations. As discussed in further detail below, the cumulative effect of the proposed rules

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[2] Again, we would support disclosure of a summary of side letter terms agreed to prior to the adoption of the rule only for open-ended funds, not closed-end funds no longer accepting subscriptions in order to minimize costs that would not clearly benefit investors.

[3] For example, PitchBook writes with respect to private equity funds that "first-time funds deliver outsized returns more frequently, deliver poor returns less frequently, and return capital more quickly." PitchBook Analyst Note: First Time PE Funds Overview, Q1 2021 PitchBook Analyst Note: First-Time PE Funds Overview | PitchBook (March 1, 2021).

(including the required reporting and inability to pass through certain expenses to investors) is likely to increase the costs of operating investment advisers, thereby raising the barrier to entry for new advisers in the space. If "seed" investment is made a less attractive proposition as well, the proposed rules could serve to materially limit the launch of new private fund advisers across the industry.

As with the prohibition on preferential transparency, we believe that this aspect of the proposed rules could have significant unintended consequences. For example, the extension of the prohibition on preferential liquidity to "substantially similar pools of assets" (and the uncertainty around such definition) could result in advisers being unwilling to launch separate investment funds with distinct but overlapping investment objectives (i.e. long-only products, funds utilizing less (or more) leverage and funds that exclude certain investments) due to difficulties in standardizing liquidity parameters across such vehicles. Advisers use varied liquidity rights as a way of managing a diverse group of investors and balanced portfolios. As previously discussed with respect to information rights, a one-size fits all liquidity profile for each fund could disincentivize the participation of certain investors with respect to each fund. Larger, more established advisers may offer less flexibility with respect to liquidity—to the detriment of investors. Overall, fewer investment options may become available to investors.

We note that the Commission is concerned that preferential liquidity that is afforded to some investors can have a harmful effect on other investors. However, similar to our views on front running above, we do not think such concerns are so great that they merit rulemaking that could eliminate legitimate and beneficial liquidity options for investors. We believe that any nefarious use of preferential liquidity rights would be better addressed as a violation of adviser fiduciary duties under the particular facts and circumstances.

Finally, this is another area where we believe that existing rights, in this case liquidity rights, should not be retroactively modified by the proposal. As mentioned above, retroactively stripping investors of rights they expressly negotiated for will disadvantage these investors, while simultaneously handing a windfall to advisers who continue to enjoy the benefit of their side of the bargain. It also seems likely that any effort to change previously negotiated rights will trigger a need to renegotiate terms, which will expose investors to significant legal costs (direct costs as well as those incurred by the adviser which are then passed along) and administrative burdens. Rather than retroactively prohibit terms that are commonly negotiated for legitimate business and operational reasons, if a summary of such terms is disclosed to all and such rules are applied prospectively, all investors will have the information they need to make prudent decisions about whether and on what terms to invest.

3. Standard of Care and Fiduciary Duties

While many advisers and industry associations have focused on the Private Fund Proposal's suggested transition from a "gross negligence" to a "negligence" standard, time constraints have prevented RFG from establishing a clear position on this important issue. We urge the

Commission to establish a dialogue with the adviser community and investors so that it clearly understands the practical implications that the industry would face if the rule were adopted as proposed. It is possible that industry discussion could shed light on certain situations where a gross negligence standard would seem more appropriate than a negligence one.

However, RFG is more concerned with the prevalence of fund documentation that includes exceptions to the duty of loyalty or similar limitations of fiduciary duty. Some private fund agreements seemingly allow the general partner and adviser to put their own interests ahead of those of the fund. For example, certain advisers have attempted to disclaim fiduciary duty or even conflicts in totality, or they have attempted to disclose all sorts of issues with a blanket waiver in the partnership agreement giving up claims relating to anything that has been disclosed. We would be in favor of restricting an adviser's ability to waive fiduciary duty in its entirety to the benefit of the adviser and its affiliates.

In addition, a common provision in private fund operating agreements allows the general partner, in one of the many instances where it is empowered to act in its "sole discretion" or "sole and absolute discretion," to take any interests into account (expressly including its own) in making such determination, which effectively undermines an adviser's duty of loyalty to a fund. We would also support a clarification that although an adviser could consider its own interests as part of a mix of competing interests, it could not weight its own interests ahead of, or equally with, those of its clients. Notably, RFG is not concerned with partnership provisions that allow a general partner or adviser, acting in accordance with the partnership agreement, to make business decisions (such as allocation of investment opportunities among clients which requires a balancing of the manager's duty of loyalty to multiple clients), provided that such decisions are necessary given the business model of the adviser and the adviser is not putting itself ahead of its clients.

It may be that, as it further reflects on this area, the Commission will determine to consider other partnership agreement terms which trigger a lack of alignment between an adviser and its clients. Likely candidates include (i) the indemnification or exculpation of a general partner or manager for breach of the limited partnership agreement or other fund documents[4] and (ii) provisions that require disqualifying conduct to be determined by a final, non-appealable decision.[5]

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[4] It is common for advisers to include contractual language wholly limiting liability for such breach (unless such breach triggers a different carveout from the indemnification protection, such as fraud), but in a typical contract the parties would naturally expect the breaching party to bear the financial consequences of its violation.

[5] Partnership agreement standards of conduct are commonly negated as a practical matter because they are conditioned on a final, non-appealable decision being reached. This rarely occurs for a variety of reasons, even after a court of first impression makes a finding of bad conduct.

4. **Proposed Rule 211(h)(2)-3(b) – MFN and Disclosure of Preferential Rights**

As discussed above, RFG supports a requirement that advisors summarize on an anonymized basis the preferential rights offered to other investors. We support this-- even if investors ultimately incur somewhat greater expenses as a result. However, to minimize unneeded expense increases, assuming the Commission does not more broadly "grandfather" existing terms, we would exempt from this requirement closed end funds that are no longer fundraising or other private funds that are no longer accepting subscriptions.

We are also concerned as to how the proposed rule's timeline, requiring disclosure of preferential treatment to prospective investors in a private equity fundraising process prior to commitment, would be implemented in practice. If advisers are required to circulate draft side letters in advance of the first closing, and subsequently entertain further negotiations (which would also need to be recirculated), the fund closings may become unreasonably long. We believe there are potential solutions to this issue, but RFG has not had sufficient time to fully address this concern with its members.

5. **Quarterly Reporting Proposals**

While we believe that the proposals on fund-level and portfolio company-level quarterly performance and expense reporting are generally beneficial, we would be in favor of certain modifications to the proposed rules (as discussed below). However, our main concern with reporting remains the restrictions on preferential transparency described above. When combined with the mandated quarterly statements, we fear that many advisers will limit the information provided to what is required in quarterly statements, thereby decreasing the overall information available to investors for such private funds.

Nonetheless we agree that these quarterly reporting proposals facilitate the validation of fees and expenses, and will fill a current gap experienced by investors in that they:

- enable investors to understand the entire amount of adviser compensation allocated or paid to the adviser and its related persons;
- provide investors with detail needed to validate that the fund expenses borne by the fund conform to contractual agreements;
- assist investors with their liquidity management and cash flow models, as they would have greater insight into the fund's projected cash flows and their obligations to satisfy future capital calls for adviser compensation with cash on hand; and
- provide investors with greater transparency into advisers' fee and expenses practices, particularly with respect to how offsets, rebates and waivers affect adviser compensation.

We strongly believe that the final rule should differentiate between liquid and illiquid private funds in terms of required reporting, and be drafted in a manner that maintains the current

market norm of monthly -- rather than quarterly S-- statements from liquid funds. Because liquid funds are generally more dynamic and can experience a greater degree of turnover, investors need to receive information on a monthly basis from such funds to properly monitor their overall portfolio strategies. In addition, we also think the reporting for liquid funds should be expanded to include certain information that would be inapplicable for illiquid funds, most notably disclosure on the soft dollar benefits received by the general partner and the adviser with respect to the fund.

As proposed these requirements would only apply to registered investment advisers, but RFG members have experienced the most difficulties getting adequate reporting from venture capital and other exempt reporting advisers. Ideally, the proposal would apply uniform reporting requirements to all private fund advisers that meet a certain threshold with respect to assets under management. Given the concern with burdening smaller advisers with a high level of costs, we believe the requirement should apply only to those advisers with assets under management that exceed a $110 million threshold.

6. **Proposed Rule 211(h)(2)-1(a)(4) – Tax Netting in Clawbacks**

We believe the proposal would be beneficial to investors insofar as it requires any overpayment of carried interest to be fully corrected. Advisers control realization events and distributions. Tax netting of clawbacks distorts the bargained for carry split, misaligns incentives and complicates reporting. We see no reason to encourage or allow overpayments.

In its release the Commission has cited the more aggressive clawback reduction formulation (Proposed Rule 211(h)(2)-1(a)(4)), which we believe is less prevalent in the industry. In the example used by the Commission, the clawback amount itself is reduced by potential or hypothetical tax amounts. The other formulation, commonly used, requires the general partner to pay the lesser of (1) the clawback amount, or (2) the total amount of carried interest received by the general partner, reduced by actual or hypothetical tax amounts. We believe that the latter formulation (which is more investor-favorable) is incorporated more frequently into private fund documents, and we think that any prohibition should also cover these provisions. With this in mind, we believe the proposal should be broadly drafted to provide that all such overpayments are subject to clawback.

7. **Proposed Rule 211(h)(2)-2 – Adviser-Led Secondaries**

The proposal to require an independent fairness opinion for an adviser-led secondary transaction may drive up costs and delay transactions but, for some private side investments, we believe these downsides are acceptable. RFG suggests the Commission modify its proposal in three respects:

- exclude situations where a fairness opinion provides little value, such as (i) funds that only (or primarily) hold publicly traded securities and (ii) transactions where the adviser has conducted an auction process and selects the bidder offering the best price;
- in other instances, require a fairness opinion in all situations where the adviser has a relationship with a counterparty, regardless of which entity may be seen as "leading" or "initiating" the secondary transaction; and
- last and most important, require advisers in all situations to use reasonable efforts to provide a "status quo" option so that investors that do not cash out remain invested on their original terms without carry crystallization. This last point would significantly benefit investors that wish to remain invested and are currently forced to choose between two options that are often both worse than the terms they signed up for when they made their initial commitment to the fund.

8. **Proposed Rule 211(h)(2)-1(a)(7) – Borrowing from a Fund**

RFG supports a blanket prohibition on the practice of an adviser (or a person directly or indirectly related to the adviser) borrowing from a private fund client, with possible narrow exceptions. Most credit markets have financial institutions which stand ready to extend credit to the adviser and its personnel for a variety of reasons, including to cover tax payments. A fund should not be a vehicle to assist advisers or their employees with their own financial matters. That capital could be better used to further the fund's legitimate investment goals.

It may be desirable to broaden the scope of the proposal beyond an adviser borrowing from a fund, but we have not had sufficient time to fully address this with RFG members. Possible extensions of the proposed rule include:

- looking beyond private funds;
- requiring more detailed disclosures such as amounts of historical borrowing, the reason for the borrow, and how quickly borrowed amounts were repaid etc.;
- exploring whether problems associated with loans by an adviser to a fund should be addressed by either requiring more transparency and/or requiring that such loans not place the adviser before investors of a distressed fund; and
- considering the benefits that might be obtained from a prohibition on the fund borrowing from the adviser or its affiliates.

On this last point, RFG believes that, given the depth of the credit markets, funds should generally be able to borrow from non-affiliates. However limited exceptions to any such prohibition might be appropriate -- such as would allow a fund to borrow (or lend) if explicitly to benefit the fund's primary investment activity or if specifically disclosed prior to an investor's commitment. This could, for example, help the fund bridge transactions in a way that is designed to benefit fund investors. Even this, however, should be subject to close scrutiny.

9. Additional Unintended Consequences

In addition to our concerns with specific aspects of the proposed rule voiced above, RFG members are also concerned about industry-wide implications of the Private Fund Rule in general. For one, we are concerned about the potential impact of the proposed rules on new advisers. We fear that the increased compliance and operating burden imposed by certain aspects of the proposed rule, when combined with the Private Fund Proposal's limitation of common practices with respect to "seed" investors, will serve to restrict the launch of new advisers, thereby depriving the industry and allocators of (i) innovation and opportunities which have historically produced attractive returns and (ii) the ability to encourage new and diverse advisers. The cumulative effect of the proposed rules -- including the required reporting and inability to pass through certain expenses to investors -- is likely to increase the costs of operating investment advisers. This will raise the barrier to entry for new advisers and lead to additional consolidation in the investment management industry, reducing competition among advisers overall.

RFG is also concerned about the potential strain that compliance with the proposed rules would place on allocators, specifically in the short to medium term. Passage of the Private Fund Proposal in anything approximating its current form would be a source of considerable disruption in the industry. This is true for investors as well as advisers. As stated above, if the final rules do not provide grandfathering for existing arrangements, it is certain that many of the arrangements that RFG members and other diverse investors have been operating under will be invalidated, or at least need to be renegotiated. That will require a substantial diversion of resources and is likely to be a material drag on the investment performance of the endowments and foundations that comprise our membership because fees may increase, and legal and compliance costs certainly will.

There are several other aspects of the proposal that we believe are generally beneficial. Specifically, we support the following proposals (in some instances with select changes):

- **Proposed Rule 211(h)(2)-1(a)(1) – Accelerated Payments:** Advisers may not charge accelerated payments to portfolio companies.

- **Proposed Rule 211(h)(2)-1(a)(6) – Non-Pro Rata Fee/Expense Allocation:** Advisers are prohibited from charging fees/expenses on a non-pro rata basis. We generally support this if the allocation is based on capital invested in a specific investment (rather than on capital commitments to the fund as a whole). This ensures that excused investors will not bear the costs of investments in which they do not participate.

- **Proposed Rule 206(4)-10 – Private Fund Audits:** Advisers are required to get annual audits for all private funds. These requirements largely codify existing practice. To

reduce unnecessary costs, RFG recommends carve-outs for funds in early start up phases or nearing liquidation, for co-investment vehicles where the asset(s) are held and valued in the main fund, and for funds of one where bilateral negotiations have occurred and should be respected. In addition, the proposed rule requires an adviser to notify the Commission upon a change in auditor or the failure to receive a clean audit. We believe the adviser should also be required to notify the limited partners of its clients upon the occurrence of such a significant event.

There are other aspects of the proposal which we have not had time to address in sufficient detail. These include the prohibition of passing compliance costs on to clients (Proposed rule 211(h)(2)-1(a)(3).) The proposal suggests that advisers may not charge investors or private funds for fees or expenses for the adviser's compliance costs or regulatory exams and investigations. While we know now that we need more clarity on what the Commission is intending – including on whether the costs of complying with all the new proposals count as compliance costs that must be borne by advisers – we believe there are potentially other costs that an adviser should bear out of its management fee. This is another topic on which we have not had the time to reach a conclusion.

More broadly, we think it likely that advisers will seek to pass on costs attributable to the rules in one way or another (most likely through increased management fees) and we are concerned that we have not had enough time to properly weigh the potential added costs against the associated benefits. We note that the Commission has asked for input on budget-based models. We believe such models where the proposed budget has been agreed to by investors should be incentivized --since they discourage the use of the management fee as a de facto additional profit center. For this reason, RFG would generally support carve-outs from the proposed rules that permit budget-based fee models to continue to be employed by the industry. Since such models are not especially common, we have not had enough time to propose a fulsome way to incentivize such models that avoids unintended consequences for investors.

We thank you for your consideration of our comments. RFG would welcome the opportunity to discuss any of the above issues further with the Commission. Please reach out to me at [redacted] with any inquiries.

Respectfully,

Deborah Prutzman,
Chief Executive Officer

cc: The Honorable Gary Gensler
The Honorable Caroline Crenshaw
The Honorable Allison Herren Lee
The Honorable Hester Peirce
Melissa S. Gainor, Assistant Director, Investment Adviser Rulemaking Office

Marc Mehrespand, Branch Chief, Chief Counsel's Office
The Div. of Investment Management