June 13th, 2022

Ms. Vanessa A. Countryman
Secretary
U.S. Securities and Exchange Commission
100 F. Street NE
Washington, DC 20549-1090
Submitted via email to rule-comments@sec.gov

Re: File No. S7-03-22

Dear Ms. Countryman:

I am the chair of the Private Investment Funds Committee of the State Bar of Texas Business Law Section. I primarily represent private fund managers that are registered as investment advisers ("**RIAs**") under the Investment Advisers Act of 1940 (the "**Advisers Act**").

I am submitting this letter in response to the request of the Securities and Exchange Commission (the "**Commission**") for comment on Investment Advisers Act Release No. 5955 (February 9, 2022), which proposes new rules and amendments to existing rules under the Advisers Act applicable to private fund managers (the "**Proposed Rules**"). The views expressed herein are my own and do not represent the views of the State Bar of Texas, its Business Law Section, the Private Investment Funds Committee, my law firm, or any of our clients.

I am grateful for the tremendous effort of the Commission and its staff in putting forward these thoughtful proposals for public input. I understand and agree with the Commission's concern with transparency and disclosure of conflicts of interest by private fund managers. Nevertheless, I am concerned that the scope of the Proposed Rules, if adopted in their current form, would have a profound negative impact on the private fund industry.

My practice focuses on the formation of private funds and compliance with the Advisers Act by fund managers. Most of my clients are managers of small to mid-sized closed-end funds. I also represent high net worth individuals, family offices, and institutional investors with respect to the negotiation of the terms of their investments in private funds.

I believe that many of my smaller clients could not afford to comply with some of the Proposed Rules. Thus, I am afraid that the Proposed Rules could create barriers to entry for new managers and cause smaller existing managers to wind down their funds and close their operations. Finally, I believe the retroactive application of the Proposed Rules would be unfair to both fund managers and their investors who have negotiated and rely on the terms of fund documents that otherwise comply with the requirements of the Advisers Act.

This comment letter will focus on Proposed Rules 211(h)(1)-2 (the "**Quarterly Statement Rule**"), 206(4)-10 (the "**Financial Statement Audit Rule**"), and 211(h)(2)-1(2) and (3) (the "**Regulatory Expenses Rules**"), particularly with respect to how these Proposed Rules would affect illiquid closed-end funds and their managers.

1. Quarterly Statement Rule

In general, I support proposed Rule 211(h)(1)-2, which would require RIAs to prepare and distribute quarterly statements to investors in each private fund they manage. Nevertheless, I believe some of the required content and reporting format of the Quarterly Statement Rule are not necessary or beneficial to investors.

I agree that a detailed accounting of all compensation, fees and other amounts paid by the private fund or a portfolio company to the fund manager or its affiliates during each quarterly reporting period would be beneficial to fund investors. I also support a detailed reporting of all fund cash flows during the quarter, including expenses charged to the fund and the distribution of proceeds from the sale of fund investments.

Most registered fund managers already provide quarterly statements to their investors, but not in the format that would be required by the proposed Quarterly Statement Rule. I believe that the reporting format required by the Quarterly Statement Rule is not necessary and is not what fund investors want. Fund managers should be given the flexibility to tailor their quarterly investor reports depending on the type and size of the private fund and the needs of its investors. In my experience some investors require quarterly reports that cover specific items in a format specified by the investor. Investors and fund managers should be given the flexibility to negotiate the format of quarterly reports.

While I generally agree with the content requirements of the Quarterly Statement Rule, I believe that quarterly performance reporting should not be required for illiquid closed-end funds such as funds of funds, private equity funds, and venture capital funds. I appreciate that the proposed Quarterly Statement Rule makes a distinction between liquid and illiquid funds with respect to performance reporting, but reporting IRR and MOIC in the early stages of an illiquid fund may be confusing and misleading to investors given that during this period, expenses are relatively high, the fund may not be fully invested, and the value of investments that are made do not materially change.

2. Financial Statement Audit Rule

Proposed rule 206(4)-10 would require RIAs to cause each private fund they manage to undergo a financial statement audit under GAAP at least annually and upon liquidation. The audited financial statements and auditor's report would need to be promptly distributed to investors upon completion. If an RIA acts as a sub-adviser to a private fund that they do not control, the RIA would be required to take "all reasonable steps" to cause the private fund to undergo a financial statement audit, even if the sponsor and manager of the fund is not registered under the Advisers Act and otherwise would not be required to do so. Finally,

the engagement letter with the independent auditor would require the auditor to notify the SEC upon the auditor's termination or its issuance of a qualified opinion.

Many of my clients do not cause each of their funds to undergo a financial statement audit, and in my experience, investors in smaller private funds, including some of my investor clients, do not require or even desire an annual financial statement audit due to the cost of such an audit and its negative impact on investment returns. These investors often negotiate other protections, such as requiring the use of an independent fund administrator to monitor all fund transactions and cash flow in real time, and requiring quarterly reporting flows verified by the administrator, as discussed above.

My clients that do not cause their funds to undergo an audit comply with Rule 206(4)-2 (the "**Custody Rule**") by engaging an independent accounting firm to conduct an annual surprise custody exam. I believe the custody exam is more effective than a financial statement audit to verify custody.

I understand the Commission's concern that a surprise custody exam does not examine valuations assigned to investments by the RIA. Generally, however, managers that manage illiquid funds do not charge fees that are based on the value of unrealized investments, nor do they market their funds based on the performance of unrealized investments.

Finally, many illiquid funds rely on audits of the financial statements of the portfolio companies and other funds they invest in. For example a fund of funds or a co-investment vehicle may rely on valuations provided by the sponsor of the investment, and the fund manager has no control over such valuations.

3. The Regulatory Expenses Rules

Proposed Rules 211(h)(2)-1(a)(2) and (3) would prohibit all private fund managers (whether registered or not) from charging their funds for compliance and regulatory expenses, including expenses related to regulatory examinations and investigations.

Many of my clients charge little or no management fee and instead pass compliance expenses through to their funds on a pro-rata basis. This arrangement has been negotiated with fund investors and both the nature of the expenses and the related conflicts of interest are fully disclosed to investors.

I agree that expenses of regulatory investigations should not be charged to a fund, unless the investigation ends without a finding that the manager or its affiliates have violated applicable law.

The Commission acknowledges that the Regulatory Expenses Rule would require fund managers that currently charge regulatory expenses to their funds to restructure their fund documents and their business model. Doing so with respect to existing funds would not be practical, however, because fund documents cannot be amended to increase management

fees to cover compliance expenses. As a result, managers would not be able to afford a robust compliance program, which in turn would be harmful to investors.

4. Retroactive Application

Finally, a retroactive application of the Proposed Rules would be unfair to both fund managers and their investors who have negotiated their current relationship. The terms of existing fund documents are negotiated between sophisticated parties and requiring the amendment of such documents would impose heavy and unnecessary burdens on private fund managers and their investors who would be required to renegotiate their business arrangement.

We appreciate the opportunity to comment on the Proposed Rules. If we can be of any further assistance in this regard, please contact George Lee at the contact information provided below.

Respectfully,

George T. Lee

cc: The Honorable Gary Gensler

The Honorable Caroline Crenshaw

The Honorable Allison Herren Lee

The Honorable Hester Peirce