

Fifth Circuit Vacates Private Fund Adviser Rules

By Joseph M. Mannon, Cody J. Vitello, Jeff VonDruska, Adam S. Goldman, Laure Sguario and David W. Soden

June 5, 2024

In a 3-0 decision, the Fifth Circuit Court of Appeals vacated the SEC's private fund adviser rules ("**Final Rule**"). Each component of the Final Rule was vacated, including the Private Fund Audit Rule, Private Fund Quarterly Statement Rule, Private Fund Adviser Restricted Activities Rule, Adviser-Led Secondaries Rule, Preferential Treatment Rule and Books and Records Rule Amendments. The original lawsuit was brought by several trade associations who sued the SEC over the Final Rule in imposition of undue regulatory burdens and costs.

In making its ruling, the Fifth Circuit found that the SEC had exceeded its statutory authority in adopting the Final Rule and found that "no part of the [Final Rule] can stand." In particular, the court held that Section 211(h) (adopted as part of the Dodd-Frank Act) applies to "retail customers" and not to private fund investors, and therefore the SEC exceeded its statutory authority in relying on that section to adopt the Final Rule. The court was also not persuaded by the SEC's argument that the Final Rule was proper under the SEC's anti-fraud authority. The court found that the SEC failed to articulate a rationale for connecting the Final Rule requirements to the prevention of fraud. As private funds are generally exempt from federal regulation on internal governance, the court found that the SEC cannot issue rules under an anti-fraud theory (using Section 206 of the Investment Advisers Act) that affects the internal governance of a fund.

It is unknown whether the SEC will appeal the ruling.

If you have any questions, please contact **Joseph M. Mannon** at jmannon@vedderprice.com, **Cody J. Vitello** at cvitello@vedderprice.com, **Jeff VonDruska** at jvondruska@vedderprice.com, **Adam S. Goldman** at agoldman@vedderprice.com, **Laure Sguario** at lsguario@vedderprice.com, **David W. Soden** at dsoden@vedderprice.com or the Vedder Price lawyer(s) you normally work with.

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