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FUNDamentals — July 2026

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FUNDamentals is a periodic digest of news and information specifically for investment funds and investment advisers. In this issue, we highlight key industry trends, the SEC's deregulatory rulemaking agenda, SEC enforcement priorities, the IRS's new guidance on self-employment taxes, updates to qualified client thresholds, ILPA's new guidance on organizational expenses, fund liquidity trends (continuation funds, secondaries, and LPs as lenders), proposed changes to Form PF, the SEC's examination priorities and recent risk alerts, developments in crypto and digital assets, and the status of the FinCEN AML rule for investment advisers.

PODCASTS

Don't forget to check out our private equity-focused podcast series ***PE Pathways***. Season 2 highlights include our "Carried Away" series (GP economics, fee developments, and carry developments). Other episodes focus on unlocking the value in distressed assets and the latest trends in the food and beverage industry.

BY THE NUMBERS

Private equity posted impressive gains in deal and exit value in 2025, as large transactions dominated the dealmaking landscape. Buyout and growth deal sizes increased, with larger deals (more than $500 million) increasing the most.

However, the first half of 2026 tells a more complex story. Deal volume in the first half of 2026 declined by more than 30%, while the average deal size rose substantially from the first half of 2025. More money is being focused on fewer deals overall, with mega-deals leading the way and the middle market feeling somewhat stalled.

Aggregate dollars raised actually increased in the first half of 2026 relative to the first half of 2025, despite a slight decline in the number of funds raised. The dumbbell shape of fundraising is continuing, however, with firms showing strong distributions to paid-in capital (DPI) raising their funds more quickly while other firms face longer fundraising periods and lowered overall targets. These numbers highlight a similar trend as seen on the deal side — more money being put to work with fewer managers.

The exit bottleneck evident throughout 2025 has not materially cleared. IPO windows remain small and unstable, strategic buyer appetite is more selective than ever, and sponsor-to-sponsor transactions face ongoing valuation mismatches. Continuation vehicles and GP-led secondaries are becoming a stronger focus for managers working to provide liquidity for their limited partners.

Health care remains the most resilient sector for PE deployment, while technology continues to struggle with AI disruptions and all sectors face headwinds from geopolitical tensions and oil price spikes.

PRIVATE FUNDS CFO: FEES AND EXPENSES SURVEY 2026

It's here! The *Private Funds CFO Fees & Expenses Survey* was launched with Troutman Pepper Locke in 2014 in response to fund managers' questions about who should pay fees and expenses. Troutman has sponsored this report, which is produced every two years, to create a benchmark to compare and review fee-related practices across the private markets industry. The 2026 edition features a survey of 132 U.S. alternative asset fund managers on their fees and expenses practices. This report shows the evolution of the industry toward a climate of transparency and examines broken-deal expenses, co-investments, and the environment in which LPs are facing an expanding set of costs. Download the full report here.

OFF-CHANNEL COMMUNICATIONS VIA TEXT, CHAT, OR PERSONAL EMAIL

In May, after the Security and Exchange Commission's (SEC) recent off-channel enforcement sweep, the Investment Adviser Association and the Investment Company Institute wrote a joint letter to the SEC urging the SEC to modernize the books and records rules to address the changed nature of communication and recordkeeping technologies, and to place greater emphasis on a firm's good faith efforts, the strength of its compliance programs overall, the presence (or absence) of any fraud or discernible investor harm, and the relative costs, burdens, and benefits of recordkeeping programs. When the SEC announced its enforcement results for fiscal year 2025, it noted that since fiscal year 2022 it had brought 95 actions and $2.3 billion in penalties against firms for books and records violations in cases that identified no direct investor harm and produced no investor benefit or protection. See SEC Announces Enforcement Results for Fiscal Year 2025. The strict liability standard is particularly evident in the case of off-channel communications (text, chat, and personal email). Even when firms required employees to use firm-issued devices for business communications, dutifully monitored employee messages under various non-firm applications, required employees to certify their compliance with policies prohibiting off-channel communications, provided regular training on these policies, and disciplined employees who violated the firm's policies, they were still sanctioned for employee violations. See In the Matter of Qatalyst Partners, LP, Rel. No. 34-101143 (Sept. 24, 2024). For more information, see the full Investment Adviser Association and the Investment Company Institute letter.

AI… AI… AI…

AI is transforming how investment advisers research markets, construct portfolios, interact with clients, and run their businesses. An adviser's obligations under the Advisers Act remain — as yet — unchanged. In considering whether and how to integrate AI into their businesses, investment advisers must consider the substantive and compliance implications of AI under the Advisers Act. For more information, see "AI Heightens Old Compliance Risks For Investment Advisers."

OUTBOUND INVESTMENTS

As our foreign investment and national security team highlighted in a recent post, there have been several important developments in this space. Most notably, the fiscal year 2026 National Defense Authorization Act (NDAA) included the Comprehensive Outbound Investment National Security Act of 2025 (COINS Act), which will make several changes to the Treasury Department's existing Outbound Investment Security Program (OISP), which we discussed in a previous issue. The COINS Act changes do not take effect until Treasury implements them in its OISP regulations, which likely will not happen until the first half of next year. The COINS Act leaves the overall structure of the OISP in place, but makes changes around the edges, such as expanding the scope beyond China (including Hong Kong and Macau) to include Russia and other "adversaries." Most importantly, the enactment of this statute by Congress shows that this "reverse CFIUS" regulatory program is here to stay, and the direction of travel is an expanding scope to cover more types of transactions and technologies. For transactions that may implicate the OISP (*e.g.*, China and certain critical technologies), it is critical to have solid diligence and appropriate terms in place from the outset.

On April 10, the Treasury Department's Financial Crimes Enforcement Network (FinCEN) and Office of Foreign Assets Control (OFAC) jointly issued a notice of proposed rulemaking setting out their view of how sanctions, anti-money laundering, and countering the financing of terrorism compliance requirements should apply to permitted payment stablecoin issuers (PPSIs) under the Guiding and Establishing National Innovation for U.S. Stablecoins (GENIUS) Act. For a deeper dive on GENIUS Act financial crimes compliance developments, see "GENIUS Act AML and Sanctions Rules for Stablecoin Issuers: A Few Surprises but Broadly as Expected."

SEC FOCUSES ON ECONOMIC CONFLICTS OF INTEREST FOR INVESTMENT ADVISERS

In June, the SEC's Division of Examinations published a Risk Alert highlighting exam observations related to investment advisers' obligations concerning economic conflicts of interest and associated fee practices. The Risk Alert signals that examiners will be taking a closer look at the economic incentives that advisers and their financial professionals may have when recommending products, services, or account types to clients, including the source and structure of compensation and other economic benefits.

The Risk Alert highlights several categories of economic conflicts that examiners have observed during their examinations of SEC registered investment advisers, including:

- Economic conflicts of interest that were undisclosed, or where the disclosures were incomplete or misleading.
- Fee practices that were inconsistent with advisory agreements and disclosures.
- Compliance programs that did not fully address economic conflicts of interest and risks.

In light of the Risk Alert, investment advisers should consider the following action items:

- Conduct a comprehensive conflicts inventory. Map all sources of revenue, compensation, and economic benefits at both the firm and individual levels that could create incentives to favor certain recommendations over others.
- Review and enhance disclosures. Ensure that Form ADV Part 2A and other client-facing disclosures clearly and specifically describe all material economic conflicts.
- Update policies and procedures. Evaluate whether existing compliance policies adequately address the identification, disclosure, and mitigation of economic conflicts, and revise as needed to reflect current business practices and product offerings.
- Train financial professionals. Ensure that personnel involved in making recommendations understand the firm's conflicts and the importance of acting in clients' best interests notwithstanding any economic incentives.

Firms that have not recently pressure tested their conflicts analysis and corresponding disclosure may find themselves on the wrong end of a deficiency letter.

Economic conflicts of interest remain a top examination priority for the Division of Examinations, and the Division has indicated that inadequate disclosure of economic conflicts is viewed as a core fiduciary concern, not simply a technical compliance shortcoming. Advisers that fail to identify, disclose, and manage these conflicts risk enforcement scrutiny and should act to rectify any potential issues.

For more information, see "FUNDamental QuickStudy: SEC Division of Examinations Issues Risk Alert on Economic Conflicts of Interest for Investment Advisers."

ILPA FOCUSES ON ORGANIZATIONAL EXPENSES

LPs Push Back on Fund Formation Costs: ILPA Calls for Cap, Cost-Sharing, and Transparency

The Institutional Limited Partners Association (ILPA) has issued new guidance taking direct aim at the longstanding practice of limited partners bearing the full cost of fund formation legal expenses — costs that have grown dramatically alongside the private equity industry itself. With PE assets under management expanding from under $550 billion in 2000 to roughly $10 trillion in 2025, ILPA argues that the original rationale for LP-borne organizational expenses — that emerging general partners (GP) simply could not afford them — no longer holds for today's large, well-capitalized managers.

ILPA's guidance proposes a three-part framework: (1) cap LP-borne organizational expenses at the lower of 5 basis points of target assets under management (AUM) or $10 million; (2) require GPs to share 50% of any costs exceeding that cap; and (3) mandate greater transparency around legal billing rates, budgets, and counsel selection, including competitive requests for proposals (RFPs) for funds targeting more than $1 billion in AUM.

ILPA's guidance also proposes explicitly treating side letter negotiations and most favored nation (MFN) processes as organizational expenses subject to the proposed cap rather than classifying these as uncapped partnership expenses.

For fund formation practitioners, this guidance signals increasing LP scrutiny of legal spend at the term sheet stage and a likely uptick in LP requests for rate schedules, budgets, and competitive counsel selection processes in upcoming fundraises.

To access the full guidance, see ILPA's "The Alignment Gap: Rethinking Costs in Private Equity Fund Formation."

TAX

Self-Employment Taxes for LPs of Limited Partnerships

Earlier this year, the U.S. Court of Appeals for the Fifth Circuit issued a split decision in favor of the taxpayer in *Sirius Solutions, L.L.L.P. v. Commissioner* on January 16, 2026, holding that the "limited partner exception" to self-employment taxes applies to a "limited partner in a state-law limited partnership that is afforded limited liability," without the need for further inquiry into the activities of the limited partner. The Fifth Circuit rejected the government's argument that the limited partner exception applies only to limited partners that are "passive investors" based on a functional analysis of the roles and responsibilities of the limited partners. For more information, see "Fifth Circuit Overturns Tax Court, Ruling in Favor of the Taxpayer in Case Evaluating Standard for Limited Partner Exception to Self-Employment Tax."

THE SEC

2026 Rulemaking Agenda

On July 7, the SEC released its latest regulatory flexibility agenda — the 2026 agenda — which is the clearest published statement to date of how Chairman Paul Atkins' SEC intends to reshape the rulebook governing investment advisers and registered funds. Every item under the Division of Investment Management rulemaking agenda is formally designated as "deregulatory." The agenda includes 38 potential rulemakings, with 36 in the proposed rule stage and 2 in the pre-rule stage. See the full text of Atkins' statement here SEC.gov | Statement on the 2026 Regulatory Agenda.

Key items from the 2026 agenda include:

Political Contribution Reform

A project to address "identified compliance burdens" with Rule 206(4)-5 under the Advisers Act, which sets requirements relating to political contributions by investment advisers. Likely focus areas include the very low contribution thresholds, the harshness of a two-year revenue forfeiture for inadvertent violations, the breadth of the "covered associate" definition, and the limited exceptions for returned contributions.

Recordkeeping Modernization

A project to propose amendments to Rule 204-2, the adviser books and records rule, to address the "appropriate scope" and "identified compliance burdens related to electronic communications." As noted above, this is an opportunity to modernize and rationalize the books and records rules.

Retail Access to Private Funds

Another project focuses on enhancing public and retail investor access to privately offered investments, paired with potential loosening of qualified client limits on performance-based compensation.

Small Entity Definition Updates

A proposal to raise the adviser threshold for being considered a “small entity” from $25 million to $1 billion in assets under management.

Examination Priorities

The 2026 Exam Priorities from the SEC Division of Examinations were the first released under Atkins. Key themes include:

- Continued focus on adviser fiduciary duties (duty of care and loyalty), with emphasis on retail investors.
- Focus on alternative investments including private credit, private funds with extended lock-up periods, and complex products such as option-based exchange-traded funds (ETFs).
- Emphasis on disclosure of fee-related conflicts from compensation structures relevant to private funds.
- Focus on newly registered advisers and those that have never been examined.
- Continued scrutiny of AI, automated tools, and emerging technologies.
- Crypto assets are NOT a standalone priority for the first time in several years.
- Private fund advisers are no longer a standalone priority but specific issues arise under other sections.

Enforcement Priorities

In May, newly appointed SEC Enforcement Director David Woodcock delivered his first public remarks at the MFA Legal & Compliance Conference, reinforcing the enforcement tone set by Atkins: “quality over quantity” and “back to basics.” Woodcock said that enforcement will remain focused on “protecting investors and safeguarding markets from real harm.”

Woodcock’s priorities include a continued emphasis on traditional fraud (offering frauds and Ponzi schemes, especially where there is significant retail investor loss), financial reporting, internal accounting controls, and disclosure violations, as well as insider trading, market manipulation, and individual accountability. Private funds featured prominently —Woodcock highlighted risks related to valuation, fees and expenses, conflicts of interest, and liquidity and suitability concerns. He also flagged ongoing monitoring of private credit, following its rapid expansion, and “active” enforcement related to investment advisers.

Two organizational signals stand out. First, Woodcock praised the SEC’s newly established Cross-Border Task Force and its focus on targeting international schemes and gatekeepers. Second, he previewed the reinstatement of the Retail Fraud Working Group, focused on retail investor protection and coordination with federal and state partners.

On cooperation, Woodcock noted the SEC “recognizes the difference” between “honest mistakes” that do not harm investors and fraudulent conduct, stating that “remedies will be calibrated accordingly.” He encouraged early, serious, and candid dialogue in the pre-enforcement stage, suggesting that a firm’s engagement with the Division may affect outcomes.

For more detailed information, see “Remarks at the MFA Legal & Compliance 2026 Conference.”

Qualified Client Thresholds

In April, the SEC issued a final order increasing the dollar-based thresholds for “qualified client” status under Rule 205-3 of the Investment Advisers Act. The Dodd-Frank Act requires the SEC to adjust these thresholds for inflation every five years. The updated thresholds took effect on June 29.

Under the revised thresholds:

- The assets-under-management test increased from $1.1 million to $1.4 million.
- The net worth test increased from $2.2 million to $2.7 million.

Qualified purchasers and knowledgeable employees continue to be deemed qualified clients without regard to dollar-based thresholds. The new thresholds apply only to advisory contracts and private fund subscriptions entered into on or after June 29, 2026; existing clients and investors are generally grandfathered.

For more detailed information, see “Order Approving Adjustment for Inflation of the Dollar Amount Tests in Rule 205-3 under the Investment Advisers Act of 1940.”

CRYPTO, DIGITAL ASSETS, AND TOKENIZATION

The SEC continues to develop its approach to crypto and digital assets under Atkins. The SEC’s Crypto Task Force, led by Commissioner Hester Peirce, is actively engaging with industry participants and subject matter experts, hosting roundtables, and working toward a comprehensive and clear regulatory framework for crypto assets.

In March, the SEC issued guidance clarifying the application of federal securities laws to crypto assets, and the Crypto Task Force has continued hosting roundtable discussions and educational sessions to advance its framework development. The SEC’s 2026 regulatory agenda also includes planned crypto rule changes for exchanges and broker-dealers.

The SEC and Commodity Futures Trading Commission (CFTC) have also issued joint statements on digital asset commodity transactions, and competition to tokenize capital markets continues to intensify, with ongoing debates over how equity securities should move onto blockchain rails.

On the legislative front, efforts to establish a comprehensive statutory framework for digital assets continue to advance, building on the CLARITY Act and related bills that seek to delineate SEC and CFTC jurisdiction over digital asset classes.

Our digital assets working group is tracking the big developments in that sector, including the GENIUS Act and how the financial sector should be thinking about financial crimes (AML/OFAC) and other compliance considerations as they enter this space, build new partnerships, or expand offerings. For a deeper dive on GENIUS Act financial crimes compliance developments, see “GENIUS Act AML and Sanctions Rules for Stablecoin Issuers: A Few Surprises but Broadly as Expected.”

For more detailed information, see our "Financial Services Industry 2025 Digital Assets Year in Review," the *Crypto Exchange* podcast episode "Turning Point for Digital Assets: 2025 Year in Review and What Comes Next," and our "Investment Management Quarterly Update."

LIQUIDITY

Continuation Funds

According to data reported by Kroll and PitchBook, continuation vehicles have tripled in deal volume since 2021, accounting for more than 10% of all PE exits in 2025. There were a record 147 continuation fund-related exits in 2025, up more than 18% from 2024. Jefferies has reported that continuation vehicles' share of sponsor-backed exit deal value was roughly 14% in 2025.

The market has come to accept continuation funds not simply as a cyclical response to liquidity pressures but as a recurring structural feature (along with secondaries) used by sponsors to deliver exits and to fundraise. The exit environment has created a backlog of companies held for more than four years that are potential candidates for continuation fund transactions.

For more on the current state of the continuation fund market, see our *PE Pathways* podcast episode on the "Evolving Landscape of Secondary Transactions in Private Equity."

COMPLIANCE

Form PF — Proposed Burden Reduction

In April, the SEC and CFTC jointly proposed sweeping amendments to Form PF designed to reduce private fund reporting burdens. The proposal represents a full-scale review of Form PF.

Key proposed changes include:

- Increasing the Form PF filing threshold from $150 million in private fund assets under management to $1 billion; and
- Eliminating certain filing and reporting obligations, and streamlining others.

The 2024 amendments to Form PF (which expanded reporting requirements) are scheduled to go into effect on October 1. The proposed amendments would modify certain of these requirements before they become effective.

For more detailed information, see "Investment Management Update – Q1 2026."

FinCEN AML Rule – Delayed Until 2028

On December 31, FinCEN issued a final rule formally delaying the effective date of the Investment Adviser AML Rule from January 1, 2026, to January 1, 2028.

The 2024 rule, adopted under the prior administration, formally defined certain registered investment advisers

(RIAs) and exempt reporting advisers (ERAs) as “financial institutions” under the Bank Secrecy Act, requiring covered advisers to establish AML/CFT programs, file suspicious activity reports (SARs), and maintain related records. FinCEN confirmed its intent to undertake a broader review of the rule during the delay period, aiming to ensure it is “effectively tailored to the diverse business models and risk profiles of the investment adviser sector.” The delay is also intended to “ease potential compliance costs for industry and reduce regulatory uncertainty.” FinCEN is coordinating with the SEC, and the jointly proposed Customer Identification Program (CIP) rule for investment advisers also remains in limbo.

For more information, see “FUNDamentals – FinCEN Delays Investment Adviser AML Rule Until 2028, Signals Revisions to Scope and FUNDamentals: Navigating FinCEN’s New AML Regulations for Investment Advisers.”

If you have other topics you would like us to explore in future editions, please reach out to our FUNDamentals editor Heather Stone at heather.stone@troutman.com.

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