



Private equity firms may face tougher scrutiny in light of recent SEC examinations revealing violations of law or material weaknesses in controls governing fee collection and expense allocation procedures among **more than half** of the 150 private equity advisers examined since October 2012.

Last week, Andrew Bowden, the director of the SEC's Office of Compliance Inspections and Examinations (OCIE), [warned attendees at the Private Fund Compliance Forum](#) that poorly-disclosed fees are among the unique "risks and temptations" uncovered during OCIE's recent review of the private equity industry. OCIE's ongoing review identified a number of common deficiencies among private equity advisers, repeatedly noting improper payment procedures for "operating partners"—the consultants and industry experts who are hired to identify growth opportunities and business efficiencies. According to Bowden, private equity firms often pay

these operating partners with investor funds or money from portfolio companies, but do not adequately disclose to investors that the partners are being paid an additional "a la carte" fee for their services. Bowden characterized these payments as "back door" fees that enable advisers to present high-profile operating partners as part of its team, while investors unknowingly foot the bill. Bowden also cited advisers who "shift" expenses from themselves to their clients during the middle of a fund's life, one "egregious" example being individuals who are presented to investors as employees of the adviser during the fundraising stage, but who have subsequently been terminated and hired back as "consultants" by the funds or portfolio companies. According to Bowden, some advisers are also billing their funds for various back-offices functions such as compliance, legal, and accounting costs, despite the fact that those costs have traditionally been included as a service provided in exchange for the management fee. Bowden said he hopes more rigorous regulation will help improve investor confidence in the private equity industry, noting that underlying investors include public and private pension funds, endowments, and foundations who have "little to no chance" of detecting wrongdoing by investment managers on their own. In Bowden's view, these issues are likely to persist if OCIE—the "eyes and ears of the Commission"—is "not on the job, doing exams in this area and spreading sunshine."

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