

FINN DIXON & HERLING

Client Alert | May 2026

SEC Raises “Qualified Client” Thresholds

Overview

As discussed in greater detail below, federally registered and some state registered investment advisers are prohibited from receiving performance-based compensation—including carried interest, incentive allocations, and performance fees—unless the client paying such compensation (or, if the client is a private fund, the investors in the private fund) meets the criteria to be a “*qualified client*” as defined in Securities and Exchange Commission (“SEC”) Rule 205-3 under the Investment Advisers Act of 1940, as amended (the “Advisers Act”). These criteria include, among others, the net worth of the client and the amount the client has under the investment adviser’s management.

The SEC has issued a final order increasing the dollar-amount thresholds for net worth and assets under management that clients must meet to be deemed *qualified clients*.¹ Registered investment advisers should plan to update client intake and subscription documents prior to the effective date of the change, which is **June 29, 2026**.

What is the Change?

The new thresholds are as follows:

- **\$1.4 million in assets under management** with the investment adviser – up from \$1.1 million. Such amounts are measured after giving effect to the investment in respect of which qualified client status is being determined.
- **\$2.7 million in net worth**, which for a natural person includes assets held jointly with the person’s spouse and excludes the person’s primary residence and related debt – up from \$2.2 million.

Background

Registered investment advisers are generally prohibited from receiving compensation from clients based on a share of capital gains or capital appreciation experienced by clients or private fund investors (generally, “performance-based compensation”). This general prohibition is subject to certain exclusions, including where the clients or private fund investors are *qualified clients*. To be deemed a *qualified client*, clients and investors must (a) meet one of the two dollar-based

¹ The order can be found at <https://www.govinfo.gov/content/pkg/FR-2026-05-01/pdf/2026-08480.pdf>

thresholds discussed above, (b) be a *qualified purchaser* as defined in Section 2(a)(51)(A) of the Investment Company Act of 1940, as amended (the “Investment Company Act”), or (c) be a *knowledgeable employee* as described in Rule 205-3(d)(iii) under the Advisers Act. The SEC is required to adjust the two dollar-based thresholds for inflation every five years. The last adjustment happened in 2021, when the assets under management threshold was increased from \$1 million to \$1.1 million and the net worth threshold was increased from \$2.1 million to \$2.2 million.

Who is Affected?

This change primarily affects registered investment advisers that receive performance-based compensation from (1) private funds relying on the Section 3(c)(1) exemption from registration under the Investment Company Act or (2) separately managed accounts (“SMAs”). In addition, many states require unregistered investment advisers that receive performance-based compensation from private funds to limit admission to investors that are *qualified clients*.

Private funds that rely on the Section 3(c)(7) exemption from registration under the Investment Company Act are expressly exempted from the prohibition on charging performance-based compensation.

The prohibition regarding charging performance compensation also generally does not apply to non-U.S. persons, meaning that, for example, an investment adviser that manages the account of a European client does not have to ensure that such client is a *qualified client*.

Grandfathering and Transition

In general, only advisory arrangements entered into with clients and investors on or after June 29, 2026 are affected by the updated thresholds. Advisers may continue to rely on the current, lower thresholds with respect to advisory contracts entered into, and fund subscriptions accepted, **on or before June 28, 2026**.

Action Items

Update Fund Offering Materials

All fund documents that reference the *qualified client* thresholds should be updated with the new dollar amounts, including subscription documents, offering memoranda, transfer agreements, and the like.

Consider Investors in Upcoming Closings

Advisers to 3(c)(1) funds should weigh whether to move anticipated closings earlier, so that they take place before June 28, 2026, to allow the adviser to avoid having to distribute updated subscription materials to investors with pending commitments.

Update SMAs and Other Advisory Agreements

All forms for SMAs and other advisory contracts that provide for performance-based compensation and reference the threshold amounts should be updated.

Update Compliance Protocols

Advisers should connect with their operations, investor relations and fund administration teams to ensure that documents are updated across the board and updated representations are obtained where needed.

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If you have questions concerning the matters discussed above, or would like more detailed information, please contact one of the attorneys below:

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