Schulte Roth&Zabel
Private Funds Regulatory
UPDATE

Valuation Issues Continue to Be an SEC Priority

August 2020

On Aug. 11, 2020, the SEC announced charges[1] against the former chief executive officer of Direct Lending Investments LLC, an investment adviser, for violating the antifraud provisions of the federal securities laws, including Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5, Section 17(a) of the Securities Act of 1933, Sections 206(1), 206(2) and 207 of the Investment Advisers Act of 1940. The SEC alleged that, for approximately three years, the CEO engaged in a scheme of inflating fund returns reported to investors, and thereby enhancing Direct Lending's management and performance fees, by manipulating the payment data for certain delinquent loans (which should have been marked down under the applicable valuation policy). The CEO had instructed the loans' providers to make payments to his funds, which created a false impression that underlying borrowers were still making principal payments on the loans; this material over-valuation allegedly resulted in Direct Lending collecting over $5 million in additional fees and in the CEO receiving unwarranted compensation. The SEC complaint seeks injunctions, disgorgement, prejudgment interest and civil penalties in connection with the CEO's alleged fraudulent activities.

*This article appeared in the August 2020 edition of SRZ's Private Funds Regulatory Update. To read the full Update, **click here**.*

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[1] *See* SEC Charges Former Principal of Investment Adviser with Data Manipulation and Valuation Fraud (Aug. 11, 2020), available here.