Private Capital in 2025

7 Things You Should Know

January 2025

Each new year brings with it the potential for change. 2025 is no different in this regard, with the potential for change being even more pronounced in light of the election results and technological developments. We transition to the Trump administration, with new leadership at regulatory agencies (such as Paul Atkins' expected confirmation as Securities and Exchange Commission (SEC) Chairman) and, for at least the next two years, single party control of the Executive Branch and both Houses of Congress. At the same time, the continued rise of artificial intelligence and other technologies serves as an agent of change in the global economy. Over the last half century, one of the hallmarks of the Private Capital industry's enduring success has been its preternatural ability to adapt to and thrive in changing business and legal environments. However, successful adaptation is not a given; it requires Private Capital participants to anticipate key trends in advance and to filter out the distractions of herd thinking. When we asked ourselves, "What should our Private Capital clients care about most in 2025?", our panel of Freshfields experts compiled the following seven topics for your consideration and business planning in the year ahead.

1 The Future of ESG and DEI

2 Private Capital Goes Retail

3 The AI Arms Race and Regulators' Attempts to Keep Pace

4 New Leadership at the SEC and how Resulting Substantive, Philosophical and Procedural Changes Will Impact Private Capital

5 Congressional Investigative Focus

6 A New Era for Antitrust?

7 The Deregulation of Crypto and Its Role in Increasingly Creative Incentive Equity Structures

1 The Future of ESG and DEI

Sam Houshower, David Nicolardi, Ginger Hervey

The coming year will mark an about-face for federal environmental, social, and governance (ESG) policy in the United States, as well as tensions between the expected federal approach versus the demands of investors and other regulatory authorities. As we discussed in our post-election ESG brief, single-party control in Washington will give Republicans opportunity to reverse course on the ESG agenda that had recently been pursued by the SEC, blue states like California, and private sector initiatives and alliances. The incoming administration, as part of its deregulatory efforts and skepticism of ESG and diversity, equity, and inclusion (DEI), will likely seek to roll back or freeze many environmental regulations, scrap DEI efforts, scrutinize industry ESG initiatives and investment approaches, and ramp up investments in oil, gas, and coal energy sources. Some of this rapid change, such as the all-but-guaranteed abandonment of the SEC's climate disclosure rule, will primarily impact public companies. The lighter regulatory touch will also impact financial institutions and Private Capital, including the likelihood that an Atkins-led SEC will not pursue the 2022 rule proposal requiring investment advisers to make disclosures concerning ESG practices. From an investment standpoint, Private Capital firms should keep an eye on the potential skirmish over hundreds of billions of dollars in tax credits and unspent funds in the landmark Inflation Reduction Act, Biden's climate and clean-energy legislation that has incentivized clean energy investments and which Trump has promised to rescind.

The change may not just be to lift regulatory demands but to affirmatively push back on ESG and DEI commitments. Thus, a challenge for investment advisers, funds, and portfolio companies will be diverging global regulatory obligations and investor expectations around ESG and DEI, as US federal anti-ESG policy creates friction with European and global regulators that continue to implement new ESG mandates and disclosure requirements. This will also play out at state level, as states such as Texas and Florida take steps to bar banks and companies with certain ESG-linked investment practices from state contracting, even as California begins requiring climate disclosures and venture capital diversity reports in 2026. Moreover, we expect the Federal Trade Commission, US Department of Justice, and Congressional committees (as discussed in topic 5 of this publication, "Congressional Investigative Focus") to investigate the ESG and DEI practices of Private Capital actors – particularly private equity funds and their advisers – for alleged collusion and anticompetitive conduct. Similarly, an Atkins-led SEC may scrutinize whether investment advisers that consider ESG and DEI factors in their investments are acting contrary to their fiduciary duties by putting their own interests ahead of those of their clients. Thus, investment advisers that choose to consider ESG and/or DEI factors in their investment activities should clearly link their consideration of these factors to their fiduciary duties to clients and ensure that their ESG- and DEI-related disclosures and policies are carefully thought through.

At the same time, there will continue to be demand for ESG- and DEI-oriented investment strategies and disclosures from certain investors, and regulators across the globe are cracking down on greenwashing and tightening requirements for carbon markets. Accordingly, Private Capital actors will need to carefully balance and manage the implications of diverging ESG- and DEI-related disclosure requirements and expectations. Likewise, ESG-related litigation concerning climate strategies and beyond continues to intensify, as chronicled in our ESG Litigation Trends Report. Finally, potential pitfalls await in the court of public opinion: companies will need to

chart a careful course with their climate and DEI efforts, as conservative activists wage campaigns targeting such efforts that can attract negative publicity and employee backlash if companies roll them back.

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Keep up with global ESG developments through our client sustainability newsletter and blog.

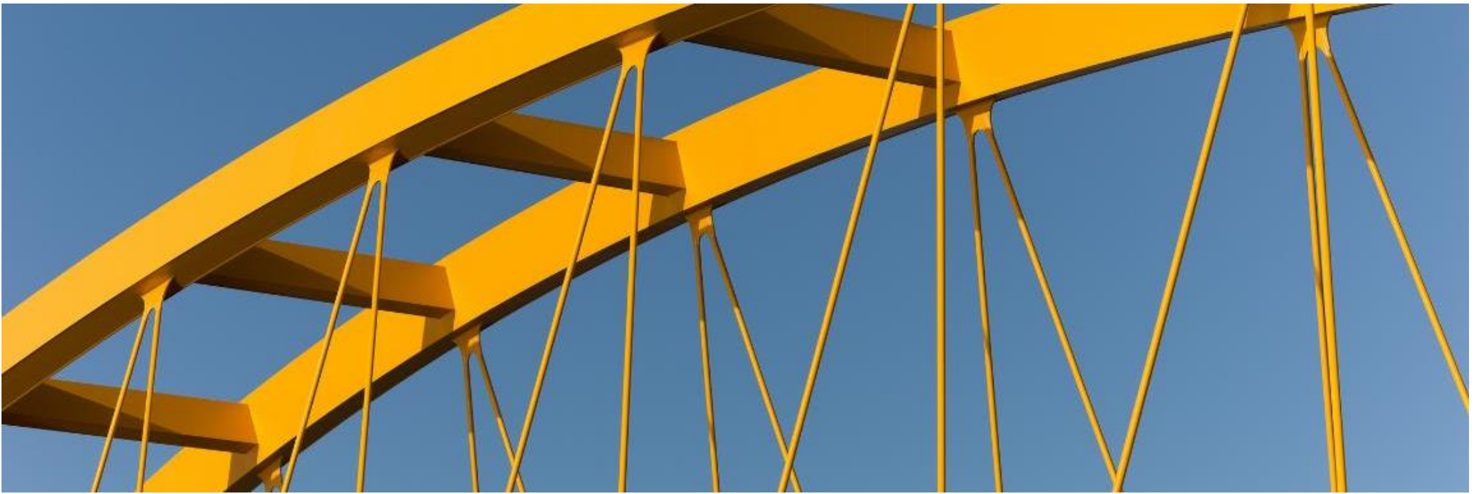
2 Private Capital Goes Retail

Ivet Bell, Melissa Hodgman

Opening retail investors’ access to Private Capital will continue to be an area of new product development for investment managers and private wealth platforms. While traditionally it has been difficult to offer private capital exposure to retail investors (mainly due to regulatory restrictions under the 1940 Act), certain existing options have gained significant traction in the past two years. These include registered vehicles that invest in private funds (including interval funds, tender offer funds and business development companies (‘BDCs’)), each of which is able to invest with differing limitations and suitability in primaries, secondaries and co-invest in private credit, private equity, real estate, and infrastructure funds. Increasingly, private fund managers are exploring in-house capability to offer and market these registered products. Separately, private wealth platforms which aggregate high net worth individuals’ capital for investment into third-party managed private funds have gained in size and number of market entrants. This ‘retailization’ trend is likely to continue gaining traction within the bounds of the existing regulatory framework.

Simultaneously there is an expectation that retail investors will likely be able to invest in new and additional ways in private funds during the incoming administration. What remains to be seen in this context is (i) what form of investment will be allowed (for example, will it be direct, indirect through a fund or other investment product, or only with the assistance of an advisor); (ii) whether there will be other limits on the investment in terms of risk; (iii) what additional, augmented disclosure and other investor protection requirements will be imposed to provide retail investors with the information required to make an informed investment decision; (iv) the means (*i.e.*, exemptive relief, rulemaking) that the SEC and other regulators use to permit such investments; and (v) what other challenges or regulatory and administrative burdens may emerge (for example, scalable reporting and managing your Know Your Customer, AML, and other record-keeping responsibilities for a larger and more diverse clientele). Guiding the approach and the resulting required disclosures, internal controls, and policies and procedures will likely be lessons learned from EU and UK regulation of private fund investment by retail investors. At the very least, you will be required to disclose material information concerning risk, valuation, liquidity, sales practices, conflicts of interests, compensation schemes, cybersecurity, and AI. Such disclosure may be less tailored and more extensive than what private funds have typically disclosed to institutional and accredited investors.

Making private funds available to retail investors is not just a US phenomenon. In both Germany and the UK, there are regulatory regimes in place which are designed to facilitate retail investment in private fund vehicles.



3 The AI Arms Race and Regulators' Attempts to Keep Pace

Brock Dahl, Eva Mak, David Nicolardi

Aggressive progress in artificial intelligence technology, and the ecosystem of innovation that AI is enabling, will be increasingly relevant to investment advisers that use AI for their investment and operational activities, private funds that invest in AI-related businesses, and portfolio companies that develop AI applications for internal or external use. To illustrate, 70 percent of private equity managers currently underwrite at least some AI-driven risks and opportunities in deals, with that number projected to increase to 96 percent in the next three years. A recent study also showed that most Private Capital targets fall short on AI readiness[1]. Now is the time to take advantage of this arbitrage opportunity.

Most Private Capital firms differentiate themselves through their operating professionals and strategies. Those professionals streamline a portfolio company's operations with each Private Capital firm's "playbook" on optimizing operations to increase profitability – its "secret sauce," if you will. As AI permeates the business and operational landscape, it is crucial for Private Capital firms to invest in operating partners who have the right mix of technology, industry, and operational expertise to use AI to turn a portfolio company with, ironically, perceived AI risks at the investment stage into a profitable company. AI is here to stay, and those Private Capital firms that can bridge the AI value gap in their target portfolio companies will thrive and capture those efficiency returns for the next decade.

The incoming administration has signaled a pro-innovation posture towards AI, prioritizing federal policies that enable a diverse group of innovators. This should generally be conducive to investing in and the use of AI by Private Capital actors, though the contours of these policies is developing and there are varying options that federal regulators can take to attempt to shape AI innovation and growth. It is possible that one or more regulatory agencies may seek to position themselves as leaders in AI regulation by developing AI-specific rules that reflect their regulatory mandates, which is the approach the SEC took under current Chair Gary Gensler. (An approach that is illustrated by the Gensler-led SEC's proposed rule that would have required investment advisers and broker-dealers to eliminate certain perceived conflicts of interest related to predictive analytics and its public focus on "AI-washing," including two settled actions against investment advisers alleging such misconduct.)

An alternative – and we believe, more likely – approach is that rather than engage in a race for regulatory dominance, federal regulators will take the cue from the incoming administration to consider how best to foster innovation while addressing core concerns through their existing and more general regulatory tools. Under new SEC leadership, for example, the proposed predictive analytics rule is highly unlikely to proceed, and we expect a more market-oriented approach that creates space for observing how AI technology impacts market participants, such as investment advisers and funds, before adopting AI-specific rules. We similarly expect an Atkins-led SEC to use existing regulations and processes to address AI and SEC exam staff to actively focus on AI-related activities that sound in more traditional abuses.

As a result, Private Capital actors should consider taking measures, based on their actual and

[1] Source: https://www.bain.com/insights/creating-value-with-ai-the-race-is-on-in-private-equity-infographic/

expected activities related to AI, to (i) catalogue their use of AI technologies; (ii) develop guidelines for acceptable use of AI technology, including human oversight; (iii) identify risks related to their use of AI technologies and establish procedures to mitigate those risks; and (iv) review their AI-related disclosures to ensure they do not overstate the potential benefits of their use of AI technology and/or understate the potential risks.

International and foreign regulatory developments are also expected to impact Private Capital investments in AI. For example, the US Outbound Investment Rule that took effect on January 2, 2025, imposes prohibitions or strict reporting requirements on direct and indirect investments by a US person in AI and certain other technology areas that involves a Chinese company. Furthermore, foreign regulatory authorities (and US states) have adopted and are expected to continue to adopt laws related to AI, which may create separate obligations depending on the jurisdictions where Private Capital actors operate and/or influence the approach and pace of US federal regulatory agencies.

For a more detailed discussion of potential regulatory approaches to AI in the US and abroad, see "AI Regulation is Evolving Globally and Businesses Need to Keep Up," Freshfields Blog Post (December 13, 2024)/Bloomberg Law (December 10, 2024).

4 New Leadership at the SEC and how Resulting Substantive, Philosophical and Procedural Changes Will Impact Private Capital

Brock Dahl, Melissa Hodgman, David Nicolardi

Over time, the change in SEC leadership will result in changes in the SEC's priorities, philosophy, and procedures. Paul Atkins, President-elect Trump's nominee to lead the SEC, previously served as an SEC Commissioner. If confirmed, Atkins' majority at the SEC for at least some of his tenure will include two of his prior counsel (Commissioners Hester Peirce and Mark Uyeda), allowing him to hit the ground running and to focus the SEC's agenda quickly on more traditional enforcement of the federal securities laws. The three have made clear in their public statements that they want to see a return to investigations and exams that are focused on protecting retail investors and/or that sound in fraud. For other areas, such as the Marketing Rule as applied to private funds and cybersecurity, we expect that while substantive changes will be subtle, the SEC will be more willing to resolve perceived deficiencies at the exam stage instead of through an enforcement action where registrants maintain an informed legal and compliance program and appropriately engage with exam staff.

Insider Trading: The more novel and aggressive insider trading enforcement actions based on substitute securities seen in the *Panuwat* case are not expected to be the norm. However, insider trading is expected to remain in the SEC's crosshairs, with enforcement actions and exams likely to be driven by evolving technology, a focus beyond trading in equities and basic options, and an expanding understanding of new and different sources of material non-public information ("MNPI") available to and at private funds.
The Commission has developed cutting-edge tools that can identify suspicious trading and other suggestive patterns across expanding data sets, including trading data for various products and social media and other public feeds. In addition, the SEC has expanded its review and monitoring of trade data well beyond stocks and bonds to include CDS, swaps, ETFs, Sector Funds, and other complex products and investments that can also be used to profit from trading based on MNPI. Finally, the Commission is increasingly aware of new sources of MNPI available to private funds. For example, a board member or board observer representing the interest of or otherwise associated with a private fund or its management is likely to have access to MNPI, which can create the appearance or actual misuse of that information when an investment decision to hold, buy, or sell is made. Private funds and their investment advisers should consider and address with proper internal controls and policies and procedures what information is available to whom given their business models, use of AI internally, and other developments or information flows that might allow internal individuals or third parties to access MNPI and misuse it.

Individual Accountability: During his prior term as an SEC Commissioner and since, Atkins focused on the need for individual accountability, in contrast to corporate responsibility. His thinking is captured in the SEC's 2006 Penalty Guidelines and statements made after his departure from the SEC, which note that individual responsibility arguably has a more deterrent effect than actions against entities, does not carry with it the same risk of additional harm to shareholders for misconduct that may already have injured them, and more appropriately addresses the actor responsible for any misconduct, *i.e.*, people, not entities, take actions. Based on this view, individuals at private funds may face more risk over the next four years of being found liable or charged with securities law violations, especially in matters involving fraud and other cases requiring evidence of intent. To address this risk,

individuals and firms should take proactive steps to ensure that they are properly protected by identifying and addressing risk appropriately, establishing and implementing systems and procedures to match their specific business models and environments, and updating both as their business models and risks evolve over time.

The Marketing Rule: Despite the change in SEC leadership and several significant judicial decisions including the Fifth Circuit's striking down the Private Fund Adviser Rules (PFAR) – which should substantially lower regulatory burdens for investment advisers to private funds and other Private Capital actors – we expect that changes related to the Marketing Rule will be less drastic. The Marketing Rule was adopted at the end of Trump's first term as President, and there is a lengthy history of SEC regulation of advertising activities by registered investment advisers, although the focus on private fund advisers is a more recent development. Furthermore, since the Marketing Rule's compliance date in the fall of 2022, the SEC has settled approximately 30 proceedings alleging violations of the Rule, and the Division of Exams has consistently identified it as an exam priority and issued multiple Risk Alerts discussing the Rule.

While substantial rollback of the Marketing Rule is unlikely, we do expect some changes in how the SEC staff interprets and administers the Rule, which will be welcomed by the Private Capital community. For example, thus far the SEC staff has taken a prescriptive approach to the methodologies used by investment advisers to private funds to calculate investment performance, even though the Rule's text and adopting release's intent afford such investment advisers with discretion regarding the specific performance calculation methodologies utilized. This prescriptive approach is illustrated by the FAQ issued by the Division of Investment Management staff in February 2024, which, as we addressed in more detail in a prior post, imposed additional requirements for what had been a common practice for investment advisers to calculate gross performance without the impact of a fund subscription facility, whereas net performance was calculated to reflect the impact of the subscription line. While, as of Wednesday, January 15, 2025, the SEC staff has not indicated plans to revisit this FAQ, a reassessment of the prescriptive approach to performance advertising in the context of Private Capital (if not a reassessment of the FAQ itself), would be welcomed and is not unlikely.

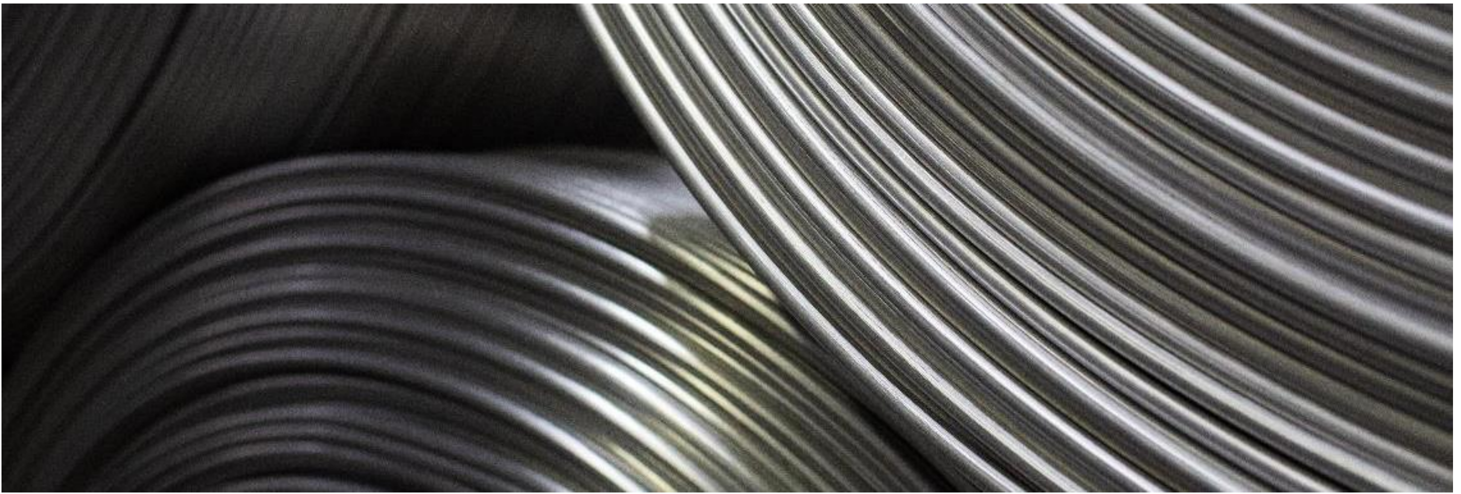
Other broader changes that we expect to occur at the SEC should impact how the SEC administers the Marketing Rule with respect to Private Capital actors. There may be more opportunities for dialogue amongst investment advisers, investors, and the SEC staff regarding marketing and presentation of performance (among other topics), plus more guidance issued by the Commission and SEC staff. Moreover, the Marketing Rule is an existing tool that the SEC may use to address perceived misleading statements or misconduct related to AI, which – as discussed in item 2 of this publication – we expect that federal regulators will initially use existing tools rather than new rules to police AI technologies.

Cybersecurity, incident response, and privacy ("Cybersecurity"): We expect an approach to cybersecurity and incident response that is less contentious for the previously stated reasons as well as less willingness by the SEC to second-guess management's reasonable determinations regarding the materiality of cybersecurity risks and events. Nonetheless, Cybersecurity will remain a crucial concern across the Private Capital sector – including investment advisers, funds, and their portfolio companies – for several reasons.

First, cybersecurity threats are expected to continue to increase in number and sophistication, and a cybersecurity incident can potentially have profound negative financial, reputational, operational, and other effects on investment advisers and private funds as well as portfolio companies in which they invest. Second, the SEC Division of Exams has consistently identified Cybersecurity as an exam priority, which is expected to continue. Third, even though the SEC's 2022 proposed rule related to cybersecurity risk management by investment advisers appears stalled, existing securities laws can already give rise to Cybersecurity-related obligations and potential liabilities for Private Capital actors.

Moreover, regulatory scrutiny of Cybersecurity is not limited to the SEC. State laws regarding privacy and incident response, as well as foreign regulators' Cybersecurity regimes, continue to expand and may impose obligations and potential liabilities on various Private Capital actors, depending on where these entities and their investors/customers are located. The evolving nature of Cybersecurity threats, the absence of a comprehensive SEC regulatory regime for Cybersecurity, and the varying approaches by different regulatory authorities heightens the need for Private Capital actors to maintain active and adaptive Cybersecurity compliance programs in 2025.

For an in-depth discussion of Cybersecurity risks and a comprehensive review of international and US state Cybersecurity regulations, see Freshfields' 2025 Data Law Trends publication.

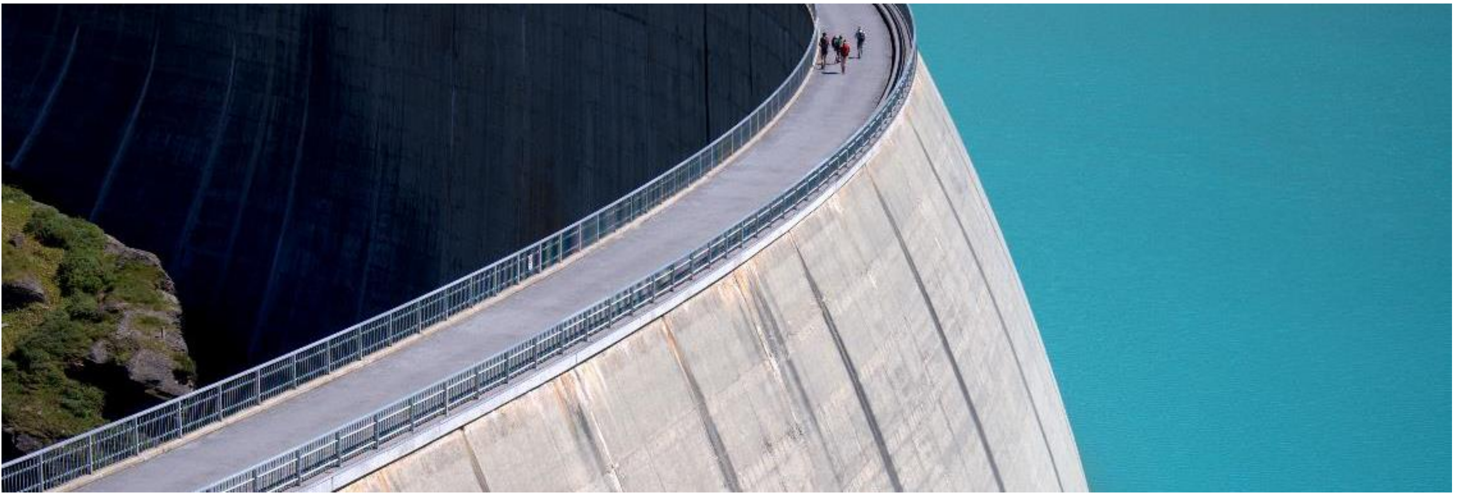


5 Congressional Investigative Focus

Andy Dockham, Austin Evers

For the first time in recent memory, private equity firms face bipartisan and sustained congressional investigative scrutiny as populist and cultural shifts influence national politics. Last Congress, House Republicans led by Judiciary Committee Chairman Jim Jordan targeted firms for their participation in global climate organizations (or, as he described, the "climate cartel"), prompting several firms to make high profile exits from these groups. Senate Democrats led by Senators Bernie Sanders and Elizabeth Warren focused on a private equity-backed hospital chain that filed for bankruptcy, which resulted in closures and alleged unexplained patient deaths. When the CEO of the healthcare company refused to testify, a unanimous Senate voted to hold him in criminal contempt – the first since 1971. Across both congressional chambers, the role of Private Capital emerged as a shared focus, with lawmakers uniting over concerns about its societal impacts, albeit through different political lenses. And the media took notice; this fertile new investigative ground led to lawmakers seeing their names and priorities in headlines.

This scrutiny is expected to intensify in 2025. Firms (and in particular, CEOs) are likely to be used as vehicles to advance broader political narratives. While Republicans and Democrats often critique private equity from different vantage points, those interests converge when investments affect constituents back home. Given Republican control of the House, the Senate, and the White House, the private sector can expect increased scrutiny (*i.e.*, committee chairs are less likely to investigate their own administration). State attorneys general have also shown interest, leading to compounded and complicated response strategies. Now is the time to proactively assess potential vulnerabilities to ensure readiness to face congressional, regulatory, and public reputational scrutiny. This is especially true for senior executives, the most likely to be called to testify before a congressional committee.



6 A New Era for Antitrust?

Bruce McCulloch, Christine Wilson

The Biden administration antitrust enforcers launched a whole-of-government approach to competition that brought a progressive enforcement philosophy to the federal antitrust enforcement agencies. The progressives emphasized new and different enforcement priorities and challenged deals using novel (or old and heavily criticized) theories of harm. Private equity companies became a specific target of the Biden administration antitrust enforcers who publicly criticized the private equity business model and sought to impede their transactions using both substantive and procedural levers.

Because the incoming Trump administration embraces certain populist goals that align with the goals of progressives, we expect certain key elements of the Biden antitrust enforcement approach to persist, including the use of antitrust to protect small businesses and workers and a sustained interest in tech companies. Notably, while the announced Trump antitrust enforcers are likely to be less hostile to commercial transactions generally (and also less hostile to the private equity business model specifically), we expect close antitrust scrutiny of deals and business conduct to continue. But we expect this close scrutiny to follow the contours of the first Trump administration, including a renewed focus on legal precedent and rigorous economic analysis and a willingness to consider sound deal remedies/divestitures.

7 The Deregulation of Crypto and Its Role in Increasingly Creative Incentive Equity Structures

Heather Brookfield, Eva Mak, Jon Fougner

The incoming administration is expected to deregulate how funds, intermediaries, and operating companies use digital assets. During the campaign, President-elect Trump promised regulatory clarity to the cryptocurrency industry. His surrogates attacked Chair Gensler for instead promulgating "regulation by enforcement." Trump has named libertarian-leaning crypto enthusiasts to key posts. We see this playing out in two ways:

- At the fund level, Private Capital managers can expect relative freedom to invest in digital assets. Paul Atkins recently spoke out against Biden's Department of Labor's opposition to crypto investing by retirement funds. In fact, since 2017, Atkins has served as co-chair of the Token Alliance, an advocacy group for the cryptocurrency industry. Brokers and platforms should enjoy increased range of motion as well. The nominee for Secretary of Commerce, Howard Lutnick, runs Cantor Fitzgerald, the investment bank that provides the liquidity to honor redemptions of Tether stablecoin – among Cantor's other crypto business lines.
- At the portfolio company level, we also anticipate increased flexibility as the President-elect's cryptocurrency czar, David Sacks, is a venture capitalist with investments in crypto businesses. Both Sacks and Lutnick have close ties to Elon Musk; Tesla still accepts Dogecoin for some products. As an example of enhanced operational freedom, the new administration is expected to accommodate employers that wish to compensate employees in part with tokens, and such flexibility may be something that private equity portfolio companies increasingly adopt as an additional type of incentive equity (alongside or as an alternative to traditional options, RSUs, profits interests, etc.) for management, employees and other service providers. We are increasingly seeing restricted token awards and restricted token units (RTUs), which largely mimic the features of traditional full-value equity awards (including vesting and lockups) in part because incentive compensation is largely tax driven, and the IRC provisions applicable to token-based compensation are the same as those applicable to traditional equity awards.

Contacts

Ivet Bell
Partner
T +1 646 343-7484
E ivet.bell@freshfields.com

Heather Brookfield
Partner
T +1 650 885-6747
E heather.brookfield@freshfields.com

Tim Clark
Partner
T +1 212 230-4620
E timothy.clark@freshfields.com

Brock Dahl
Partner
T +1 202 536-6002
E brock.dahl@freshfields.com

Andrew Dockham
Partner
T +1 202 878-9341
E andrew.dockham@freshfields.com

Austin Evers
Partner
T +1 202 921-8824
E austin.evers@freshfields.com

Melissa Hodgman
Partner
T +1 212 284-4932
E melissa.hodgman@freshfields.com

Eva Mak
Partner
T +1 408 506-6035
E eva.mak@freshfields.com

Bruce McCulloch
Partner
T +1 917 535-9513
E bruce.mcculloch@freshfields.com

Christine Wilson
Partner
T +1 202 934-9801
E christine.wilson@freshfields.com

Sam Houshower
Counsel
T +1 650 480-0200
E sam.houshower@freshfields.com

David Nicolardi
Counsel
T +1 202 923-7742
E david.nicolardi@freshfields.com

Jon Fougner
Senior Associate
T +1 650 388-0368
E jon.fougner@freshfields.com

Ginger Hervey
Associate
T +1 646 413-0728
E ginger.hervey@freshfields.com

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