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Client Alert: SEC Raises “Qualified Client” Thresholds

By: Diana M. Alsabe

On April 28, 2026, [the U.S. Securities and Exchange Commission \(SEC\)](#) issued a final order increasing the financial thresholds used to determine whether a client qualifies as a “qualified client” under Rule 205-3 of the Investment Advisers Act of 1940.

These inflation-based adjustments affect when investment advisers may charge performance-based compensation, including carried interest and incentive fees.

The updated thresholds took effect on June 29, 2026 and apply to new advisory contracts and investors admitted on or after that date.

What Is a “Qualified Client” Under Rule 205-3?

Section 205(a)(1) of the Advisers Act generally prohibits registered investment advisers from charging fees based on capital gains or capital appreciation (i.e., performance fees). However, Rule 205-3 creates an exception for advisory clients that meet the definition of a “qualified client.”

This standard, determined based on satisfaction of certain dollar thresholds, is intended to ensure that clients subject to performance fees have sufficient financial sophistication and resources to evaluate and bear associated risks.

What are the Updated Qualified Client Thresholds?

Pursuant to the Dodd-Frank Act, the SEC must adjust qualified client thresholds for inflation every five years.

Effective June 29, 2026, a client or private fund investor qualifies if they meet either of the following tests:

1. **Assets Under Management Test:** Increased from \$1.1 million to \$1.4 million with the adviser (measured immediately after entering the



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- advisory arrangement); or
2. **Net Worth Test:** Increased from \$2.2 million to \$2.7 million (excluding primary residence and related debt, but includes spousal assets).

A client satisfying either test may be charged performance-based compensation.

Note that certain categories of investors, such as “qualified purchasers” and knowledgeable employees of the adviser continue to be deemed “qualified clients” without regard to these dollar-based thresholds.

When did the Updated Qualified Client Thresholds Take Effect?

The revised thresholds apply only to advisory contracts entered into, and clients or investors admitted, on or after June 29, 2026. Existing advisory relationships and investments are generally not required to meet the updated thresholds.

Advisers may continue to rely on the prior thresholds for investors admitted before June 29, 2026, but must apply the updated thresholds for any new investors admitted thereafter.

Who is Most Impacted by the Updated Qualified Client Thresholds?

The updated thresholds are most relevant for:

- Private funds relying on Section 3(c)(1) of the Investment Company Act (i.e., funds with 100 or fewer beneficial owners), where each investor must independently satisfy the qualified client test for performance-based compensation;
- Separately managed accounts where the client is not otherwise exempt from the performance fee restrictions;
- Registered investment companies and similar vehicles where look-through treatment applies for purposes of determining the “client”;
- State-registered advisers in jurisdictions that incorporate Rule 205-3 by reference, who should confirm whether corresponding state law requirements apply; and
- Exempt reporting advisers relying on state private fund adviser exemptions, many of which require adherence to the qualified client standard.

For these structures, failure to properly apply the qualified client test can result in impermissible fee arrangements under the Advisers Act.

As an Investment Adviser, What do I Need to Do?

In light of the effective date, investment advisers should consider taking the following steps:

- Update offering and subscription documents (including investor questionnaires) to reflect the revised thresholds;
- Review advisory agreements to confirm that performance fee provisions align with the updated standards;
- Confirm whether applicable state law incorporates Rule 205-3 by reference or otherwise imposes qualified client requirements for state-registered advisers;
- For exempt reporting advisers relying on state private fund exemptions, verify whether those exemptions require adherence to the qualified client standard;
- Assess timing of fund closings and investor admissions to determine whether the prior or updated thresholds apply; and
- Revise compliance policies and procedures to ensure consistent application of the new thresholds going forward.

Key Takeaways

The SEC's 2026 inflation adjustment modestly raises the financial thresholds for "qualified client" status, narrowing the pool of investors eligible to be charged performance fees. While the changes are mechanical in nature, they carry important operational implications for private fund advisers, state-registered advisers in states that incorporate Rule 205-3 by reference, and exempt reporting advisers relying on state private fund exemptions that require adherence to the qualified client standard.

Advisers should take proactive steps now that the June 29, 2026 effective date has passed to update documentation and procedures and ensure continued compliance with Rule 205-3.

If you have questions about the changes to the qualified client threshold and how it may affect you, please contact [Scott Stokes](#), [Thomas Bilodeau](#) or [Diana Alsabe](#) at Rich May, P.C.

Disclaimer: This summary is provided for educational and informational purposes only and is not legal advice. Any specific questions about these topics should be directed to attorney(s) [Scott Stokes](#), [Thomas Bilodeau](#) or [Diana Alsabe](#).

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