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Private Equity Fund Formation - Latest Regulatory and Market Trends

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January 3, 2017 | **CORPORATE**

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Private Equity industry experts met in New York City on October 20, 2016 to discuss several key topics that have an impact on fund managers across the spectrum. Several firms that provide industry leading services to Private Fund Managers lead the discussion - Lawrence Vincent (Accordo), Jay Maher (PE Fund Administration), Tom Angnell (Withum Smith & Brown), and John Koeppel (Lippes Mathias Wexler Friedman LLP). Below is a summary of some of the items discussed at the event.

Conduct Annual Review of Your Fee, Expense Disclosures

As expenses and fees come under intense SEC scrutiny, attendees recommended incorporating a review of all your LP disclosures surrounding fees and expenses in your annual review. The attendees agreed that focus should be on your current policies, not to get to focused on pass practices that have already been accepted within your legal documents. It is critical to have your current **Expense Policies Properly Documented** and communicated to your investors. "Make it positive for the LPs" one attendee says, "communicate with your LPs through quarterly reports and at your annual meetings". Discuss the policies and offer explanations. If you need to amend a past practice, explain it and how it benefits the LPs going forward. Any past amendments should be analyzed on a case by case basis with legal advice. It was discussed to be careful how certain partners are listed on the GPs management team. If they are listed in the offering documents and website as part of the Management Team, and then are consulting for a portfolio company and charging the portfolio company, this can be an issue with the SEC if it was not disclosed as such. That could be misleading the investor that their fees to the GP are paying for that expertise. Documentation of your expense allocation policies and frequent review are the key points here. Once of the sponsors mentioned: "Whatever your policy is, your portfolio company should know it, your investment managers should know it, everyone in the organization, and all the out-source relationship should know it, so that everybody follows it. And then you can have that documentation that's going to be sent out to everybody. And then it becomes a part of your annual review."

Get Ahead of Form ADV changes

The changes come into effect in March 2017. The intention is to improve the depth, quality, and ultimately, the usefulness of the information that the advisor, clients, and the SEC receive. The message during the discussion is to **Get Ahead** of the changes, find out who you need to involve now so there's no surprises down the line. Social media plays a key role in all aspects of business these days, government filings are no different. "Social media, the internet, see what your firm is putting out there and ensue there is proper documentation and it reconciles to your filings" states one of the event sponsors. Understanding your process to collect the data points is critical along with consistent reporting.

Think Through the Allocation of Co-Investment Broken Deal Fees Well – and Upfront

The trend in co-investments has been and is increasing for a variety of reasons. LP's are attracted to certain deals and it helps them negotiate overall lower fees with the GPs. The GPs get to make the larger deals happen while keeping their fund diverse. The key here again is more disclosure. The larger LPs will always have preference, and the GPs need to clearly define and document the co-investment policies. An LP doing a co-invest deal needs to ensure the co-investment vehicle will have deal allocation policy between a fund and co-investment vehicle. Make sure you also give the same thought to the allocation of broken deal fees. "Who takes the hit when the co-investment LPs don't step up to the plate, or the deal breaks down?" **Plan it well** in advance and provide a flow chart detailing, explicitly, who pays what when that happens. Then again, communicate it thoroughly.

Seed Your Portfolio

Emerging managers are facing an exceptionally competitive fundraising environment across the alternatives space but there are some things that help gain traction among LPs. Differentiated strategy is essential, but even more fundamental is to seed a fund with transactions and to have an anchor investor, "without an anchor it's virtually impossible to raise a fund". LPs want to see the full track record of the firm, which can be difficult with no attribution. The seeded portfolio helps illustrate the strategy and execution of the team. Investors also want to see that the managing partners of the GP are putting skin into the game. New managers are differentiating themselves by continuing to get narrower with their investment focus. One of the discussion sponsors said "I'm always amazed about how narrow the strategy is. Now it's not just real estate, its hotels. It's not just hotels, its luxury. It's not just luxury, it's renovation of luxury properties." Being focused at what you are good at and if you have pipeline of deals will help secure commitments.