

Investment Management and Hedge Funds: What's Happening Now?

-- *Best Practices in Capital Raising*

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Agenda

- ▶ Private Placements
- ▶ Register Funds
- ▶ Platforms

Private Placements

- ▶ Securities Act of 1933, as amended general rule – Section 4(a)(2)
- ▶ Regulation D Safe Harbor
 - “Friends and family”
 - JOBS Act *“relaxation”*

Regulation D

- ▶ Must file Form D with the SEC
- ▶ May need to file with states under Blue Sky Rules
 - Look for institutional and *de minimis* self-executing exemptions
 - Unlimited number of accredited investors
 - Limited number of unaccredited investors
 - Must overlay Investment Advisers Act Rule 205-3 – for the manager to be allowed to take a performance fee or performance allocation (i.e., a share of profits), all investors must be, at a minimum, qualified clients, or qualified purchasers

Regulation D

- ▶ JOBS Act regulations effective 9/23/2013, allows a “general solicitation within the context of a private placement”
 - Must file Form D and elect 506(c)
 - Must have and retain evidence that all investors are in fact accredited – cannot rely on a mere representation of an investor
 - QC/QP status: does NOT trump the verification requirement
 - 100 investor limit still applies for 3(c)(1) funds
 - Uptake has been slow
 - Funds afraid of recordkeeping requirement and verification requirement
 - Are investor representations “reliable?”
 - Document delivery with virtually instantaneous DocuSign turnaround??

Regulation D

- ▶ Jobs Act Openings (continued)
 - Can use first two pages of tax returns
 - Can get a letter from a broker, investment adviser, financial advisor, lawyer or accountant
 - Can use publically available information like news reports, 10K's, etc.
 - Same rule applies to investors driven by brokers and placement agents
- ▶ Why?
 - Leap frog the gatekeepers
 - Fix foot faults
 - Bring regulatory compliance in line with practice

Regulation D

- ▶ “Friends and Family”
 - No general solicitation
 - No mass emails
 - No publicity at all
 - No open website (may have one for the adviser provided it is registered with the SEC or a State)
 - No performance table listings
 - No “freebie” if you use a registered broker dealer as your placement agent – they are under the same rules – they just have more “friends”
 - No sales to a new acquaintance until 30 days after first contact

Sales of Services vs. Sales of Securities

- ▶ Sale of Advisory Services vs. sale of an interest in a fund (i.e., a security)
 - Why registration with a state or the SEC as an adviser is so important

Use unlicensed finders? No!

- ▶ Placement Agents must be licensed as a broker dealer or be a registered representative of a licensed broker dealer
- ▶ Rescission liability on the company/fund
- ▶ Affirmative defense on payment of fees
- ▶ Aider and abettor liability

In the Matter of BLACKSTREET CAPITAL MANAGEMENT, LLC and MURRY N. GUNTY

- SEC Press Release 2016-100
- Washington D.C., June 1, 2016—
- *The Securities and Exchange Commission today announced that a Maryland-based private equity fund advisory firm and its owner have agreed to pay more than \$3.1 million to settle charges that they engaged in brokerage activity and charged fees without registering as a broker-dealer and committed other securities law violations.*
- *An SEC investigation found that Blackstreet Capital Management and Murry N. Guntly performed in-house brokerage services rather than using investment banks or broker-dealers to handle the acquisition and disposition of portfolio companies for a pair of private equity funds they advise. Blackstreet fully disclosed to its funds and their investors that it would provide brokerage services in exchange for a fee, yet the firm failed to comply with the registration requirements to operate as a broker-dealer.*

Broker Dealers

- ▶ Must be licensed with SEC and a member of FINRA
- ▶ License of “person” must be active (“U-4’d” with a licensed broker dealer)
- ▶ Person holding a series 7 license but who is “between” brokers is inactive and cannot be paid a commission
- ▶ All fees must be paid to the licensed brokerage **firm (not the individual)**
 - Cannot pay a representative directly even with consent
 - that is “selling away” and a huge violation
 - Why is selling away so bad?

Fee Arrangements with Internal Personnel

- ▶ Need to comply with either issuers' exemption ('34 Act Rule 3a4-1)
 - or
- ▶ Cannot be paid a commission or bonus tied to raising capital
 - or
- ▶ Must be a U-4'd representation of a broker dealer and all sales commissions must be paid to the broker dealer (who will then split with the representative)
- ▶ Caution – merely having a B/D “somewhere” on a business card or in a family tree is not enough
 - B/D license is not “rentable”
- ▶ Use of foreign directed parallel funds

Registered Funds

1. Closed End Funds – sales are through licensed brokers (40 Act requires a licensed underwriter)
2. Make sure any commissions are fully disclosed and not disguised advisory fees
3. Open End Funds' 12b-1 fees are strictly limited
4. Managers can use their legitimate profits and resources from other sources to pay for certain distribution related services so long as disclosed and passes the Gartenburg test

Platforms

1. Angelist – uses a combination of the issuers exemption and the JOBS Act
2. Some platforms preclear investors as accredited and qualified clients
3. Even if the platform is registered as a broker dealer itself, there are other considerations:
 - a) Remember – your fund is not a registered security AND the available exemptions to the publicly traded partnership limitations under the Internal Revenue Code are real and threaten violators with entity level corporate taxation
 - i. qualified matching services OK
 - ii. certain one-off transactions can work (very fact specific)
 - iii. general partner or managing member must stay involved and approve any transaction

The Importance of Your Fundraiser

- ▶ Already knows the investors – not making cold calls!
- ▶ Has a good reputation with the investors
 - Has shown them good funds before
 - They take his/her calls and read the fund docs
 - This is critical as investors get hundreds or thousands of pitches a year! Many are never read!

Matching the Correct Fundraiser with Your Fund

- ▶ He/She knows the appropriate investors for your fund AUM – e.g., not pitching huge public pensions for a small emerging manager (unless the investor has a dedicated emerging manager program!)
- ▶ Has deep knowledge of your fund's investment strategy – investors hate when the fund salesperson cannot answer investment questions!

Pros and Cons of Internal Fundraiser vs. Third-Party Marketer

- ▶ Internal typically devotes full-time to your fund
 - Will better know the fund, team and strategy
 - Will be “in the trenches” with you in both good and bad times
- ▶ External TPM may cost less up-front, but usually is not full time
 - TPM often represents many funds
 - TPM often pays most attention to the largest funds and “easier sell”

Fundraiser Best Practices and “Tricks of the Trade”

- ▶ Always ask your investors what they are looking for – so you can better match investors with funds
- ▶ Make sure that you get to know not just the CIO, but also the analysts – because they do the first read and make the recommendation whether to invest
- ▶ Be certain that you forward docs to the correct analyst based on type of strategy
 - Hedge funds vs. private equity
 - Many investors further break down by strategy (e.g., long/short equity, quant, private debt, etc.)
- ▶ Know and keep track of which investors prefer email (most) and which ones like to chat (some)
- ▶ Try to intersperse periodic calls with emails – usually about once every 4-8 weeks
 - If more frequently you are a pest
 - If less frequently the fundraise drags on too long

Fundraiser Best Practices and “Tricks of the Trade” (cont.)

- ▶ Put in the email subject line the name of the person to whom you are writing
- ▶ Don't send too many docs with the first email
 - Investors have too much on your plate
 - If you save a good fund doc for later, you have a reason to email again in the future
- ▶ If you have a great track record, give some bullet points about it in the email
- ▶ Do NOT simply send docs and periodic updates and say “see the attached.” – Investors get hundreds or thousands of pitches and are much more likely to read your docs if there is a solid teaser in the email.
- ▶ Get to know the administrative assistants at all of your investors – they often can be very helpful in getting your fund documents read and calls/meetings on the calendar!

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- ▶ Concentrates his practice in securities law, particularly in representing investment management companies and other clients on matters arising under the Investment Company Act of 1940 and the related Investment Advisers Act of 1940, and broker dealers and commodity futures traders and pool operators
- ▶ Represents many hedge funds and other alternative investment funds in fund formation, investment and compliance matters, including compliance audits and preparation work
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- ▶ Expert re Hedge Fund and Private Equity Fundraising, Marketing and Investor Relations
- ▶ Managing Director, Crawford Ventures, Inc. (2004-present) (raises very substantial institutional investor and family office capital for hedge funds and private equity funds)
- ▶ Longstanding Relationships with Hundreds of Institutional and Family Office Investors (B/D platforms, endowments, foundations, funds of funds, insurance companies, multifamily offices, pensions, seeders, single-family offices, sovereign wealth funds)
- ▶ Twice Elected to the Hedge Fund Association (“HFA”) Board of Directors (2014-present)
- ▶ Honoree and Recipient of the “Young Leadership Award” at the 2011 Hedge Fund Summit
- ▶ Prominent Guest Speaker and Interviewed as an Expert Regarding Successful Fundraising (including at/by Asset TV, FundFire (Financial Times), Hedge Fund Association, Hedge Fund Summit, Montclair State University, Rothstein Kass (acquired by KPMG), Seton Hall University)
- ▶ 2,000+ LinkedIn Endorsements as a Finance and Fundraising Expert, Received from his Hedge Fund, Private Equity and Wall Street Peers
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- ▶ Responsible for overseeing and executing North Street Global's strategic growth across its individual business lines both organically and through acquisition
- ▶ North Street Global's fund services group is the only Fund Administrator to have a capital introduction team for its clients inclusive of its administration product
- ▶ North Street Global services its client assets across the U.S. through its offices in New York City, Los Angeles and Miami
- ▶ Mr. Mascioli is also the Chairman of the Cap-Intro EAST & WEST Conferences - two large multi-day conferences bringing alternative asset Fund Managers and Investors together.



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