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Key Fundraising Issues: Placement Agents

Robert Bramnik
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Overview

- The basic role of a placement agent is to raise as much money as quickly as possible for a fund manager.
- The actual arrangements vary according to the jurisdiction, the fund and the manager involved.
- Newer fund managers and those investing in a new region or sector may rely more on placement agents.

Main Role

- Placement agents generally introduce fund managers to potential investors.
- They will also target suitable investors for a particular fund.
- Can be generalist or specialist agents.

Marketing

- Placement agents will typically also offer services assisting with marketing materials.
- Notable documents upon which they can advise are the PPM sent to potential investors and the presentation deck of slides for in-person meetings with potential investors. They may also advise on the form of company documents (*i.e.*, Limited Partnership Agreement) in areas not covered by the PPM.

Strategy

- Placement agents will also help fund managers with such issues as suitable fund size, negotiation of track record attribution with previous employers etc.
- More commonly used by newer fund managers.

Negotiating

- Placement agents may also offer advice on market terms, investor requests etc.
- More commonly done by other advisers.

Types of Agent

- Placement agents may be large, global firms or smaller niche firms.
- The niche firms usually specialize in one sector or location, e.g. energy or the Far East.
- In some locations, local assistance can be important.

Fees

- Placement agents usually expect to be compensated based on the percentage of new money raised.
- Terms vary but around 2.5% is the norm.
- Fee usually financed over 1-2 years.

Recent Developments

- Internal investor relations becoming more common.
- Development in this area has led to placement agents having more of a defined role, e.g. a targeted group of investors.
- Less assistance now sought on marketing, strategy and negotiation.
- Increased global regulation.

REGULATION – UNITED STATES

Overview

- As a general matter, any person who is compensated, directly or indirectly, for soliciting, offering, arranging or selling any security (including a private fund) to a United States person is required to be registered as a broker-dealer (“BD”) with the Securities and Exchange Commission (“SEC”) and become a member of the Financial Industry Regulatory Authority (“FINRA”).

Overview

- “The term “broker” means any person engaged in the business of effecting transactions in securities for the account of others.”
§ 3(a)(4)(A) Securities Exchange Act of 1934, as amended (the “34 Act”).”

Overview

- The issue of BD registration is independent of the nature of the offering. An offering of a *private fund* may be exempt from the registration requirements of the Securities Act of 1933 (for example, by virtue of Regulation D), but a person/entity that is compensated for soliciting/introducing prospective investors is still subject to the BD registration requirements.

Exceptions

A. The Issuer Representative

- One well-established exception to the general BD requirement is for persons who are officials of the “issuer” and who do not receive special compensation tied to their sales or marketing activities. See 34 Act Rule 3a4-1. The “issuer” of a fund would include its general partner(s) or a managing member (if the fund is an LLC, rather than an LP).

Exceptions

- If the fund structure includes a “manager” within the fund, it would be included as well.

An individual employed in a management role within any of these entities could qualify for the “issuer representative” exemption from BD registration.

- To qualify, the relevant individual must be regularly employed by the issuer in a capacity other than sales or marketing of the fund and must have no relevant disciplinary history. In addition, a person may only serve as the “issuer representative” for a single issuer.

Exceptions

- However, an “outside” investment manager or adviser that guides the portfolio transactions of the fund for compensation (whether in the form of a management fee and/or incentive compensation) would not be deemed to be “the issuer” and its agents would not be deemed “issuer representatives.”

Exceptions

B. Finders

- There is no generic “finder’s exemption” to the BD registration requirements and the SEC Staff has been reluctant to issue any relevant “no action letters.”
- *See, e.g., John W. Loofbourrow Associates, Inc., SEC No-Action Letter (June 29, 2006)* (no-action relief denied where mortgage broker proposed to receive a share of commissions earned by registered broker-dealer in exchange for only introducing potential investment banking clients to broker-dealer)

Exceptions

- *Hallmark Capital Corporation*, SEC No-Action Letter (June 11, 2007) (no-action relief denied where finder would receive transaction-based compensation in exchange for a range of services);
- *Brumberg, Mackey & Wall, P.L.C.*, SEC No-Action Letter (May 17, 2010) (no-action relief denied where proposed finder would effectively “pre-screen” potential investors, “pre-sell” securities to gauge investors' interest, receive compensation directly tied to successful investments, and have a “salesman’s stake” in the proposed transactions).

Exceptions

- There have been a few fact-specific circumstances for which no-action relief has been available to “finders” and brokers in a number of M&A Transactions (see *M&A Brokers*, SEC No Action Letter, January 31, 2014, revised February 4, 2014). However, the threshold conditions of this no-action letter renders it unavailable to private fund offerings.

Exceptions

- It is generally thought that a person who merely introduces a prospective investor to an issuer, and who does not review or negotiate any of the offering or business terms of a proposed transaction on a “one off” basis is not required to register as a BD. However, the offering terms of all funds will necessarily be set by the time that a would be “finder” introduces the prospective investor to the fund.

Exceptions

C. *Foreign Transactions*

- The offer and sale of a security (including a private fund domiciled in the United States) exclusively to non-United States persons (even if the transaction is solicited by a United States person) is outside of the US federal securities laws – including the BD registration requirements. (But consider foreign regulatory requirements.)
- The SEC had historically asserted extra-territorial jurisdiction over US persons who offered and/or sold securities anywhere in the world, even if all offers and sales were made outside of the US. This assertion was codified in the Dodd-Frank Wall Street and Consumer Protection Act.

Exceptions

- However, this assertion and its statutory support were challenged and ultimately rejected by the US Supreme Court in *Morrison v. National Australia Bank*, 561 U.S. 247 (2010). *Morrison* related to the sale of a United States domiciled mortgage servicing company to (solely) Australian investors. Transactions effected wholly outside of the US to non US persons are not covered by US law.

REGULATION – EUROPE

General

- In most jurisdictions placement agents from private funds are likely to be subject to some kind of regulation.
- For example, in the UK they must be regulated by the Financial Conduct Authority.

Europe

- The European Private Equity & Venture Capital Association (“EVCA”) has issued a Code of Conduct for placement agents – most European placement agents will state they adhere to this.
- Part of the Code of Conduct involves being properly regulated in the relevant jurisdiction.
- The Alternative Investment Fund Manager’s Directive (“AIFMD”) also impacts European placement agents.

Europe

- Although placement agents are unlikely to be fund managers under AIFMD they will probably be “investment firms” in most jurisdictions.
- This means that they can only market an AIF if its AIFM is entitled to do so in the relevant jurisdiction.
- Going forward this will also impact placement agents seeking to market funds with non-EU managers.

Further information

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