



Trends & Issues in Fund Terms

Presentation to ILPA – Cimarron Latin America LP Roundtable

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Agenda

- Today's Fundraising Environment
- ILPA 2.0 (released 01/11/11)
- Certain Issues Related to PE Investments by Non-U.S. Investors
- Other Issues
- Q&A

* We would like to have an open discussion with lots of audience participation. Please ask questions!



The Fundraising Environment Has Shifted

- For an array of reasons, including lack of capital, LPs have been making fewer commitments and/or smaller commitments
- However, there are new entrants exploring the asset class globally
- LPs are getting tougher on terms, specifically management fees, carried interest and key person/termination provisions
 - Significant LP focus on alignment of interests
- Even terms of legacy funds are being scrutinized
 - Re-underwriting of relationships
- GPs also find themselves addressing concerns related to pay-to-play, Dodd-Frank and other regulatory issues



ILPA 2.0

- More Realistic
- More Flexible
- More Context and Explanation
- Best Practices rather than Model Terms
- Standardized Reporting Templates
- GP Carry Clawback appendix
- Retreat on certain controversial proposals
- Acknowledgement of Influence



ILPA 2.0 – Primary Issues

- Fund Size
- GP Contribution
- Management Fees
- Carried Interest
- GP Clawback
- LPAC Governance
- Key Person and other LP Remedies



Fund Size/GP Contribution

- Duration of fundraising: nearly 40% of the funds raised in 2008 and early 2009 sought to extend their initial fundraising period (*Dow Jones Terms & Conditions Report*).
- GP Contribution: pressure to increase from 1% but data not yet supporting a trend
- Minimums to close and premiums for “first movers”
- Cornerstone LP terms becoming more common
- LPs want to see real “skin in the game” from the fund Sponsor and the senior investment team



Management Fees

- A contentious issue, due to larger fund sizes in recent years and the number of funds that some firms are actively managing
- LPs have been pushing for fees to be reduced
- Only a handful of firms have budgeted management fees – will this increase?
 - LPs seeking, at a minimum, more transparency from GPs with respect to how management fee revenues are allocated
- GPs dealing with reduced cash flows attributable to smaller fund sizes and lower fees
- On the other hand, GPs will have increased overhead costs due to increased regulation (Dodd-Frank, etc.)



Carried Interest

- Pressure to reduce carried interest percentage
- Total fund vs. deal-by-deal
- Preferred Return steady at 8%
- LP pressure leads to novel structures
 - Higher carry with lower fee option
 - Variable carry based on IRR hurdles



GP Clawback

- Interaction with distribution scheme
- Timing of GP Clawback
- Escrows
- Personal Liability (and joint vs. several)
- Interaction with LP Clawback



LP Advisory Committee Governance Issues

- What is the appropriate role for an LPAC?
- Conflicts of Interest
- Investment Restrictions
- Standard of care and indemnification
- Implied covenant of good faith and fair dealing
- Fiduciary duty to Fund?
- Fiduciary duty to other LPs?



Key Person and Other LP Remedies

- Triggers
 - Key Person
 - For Cause
 - Definition of “Cause” critical
 - “No Fault”
- Remedies
 - Suspension / Termination of Investment Period
 - Termination of Fund
 - GP Removal
 - GPs resisting “no fault” removal
 - Economic impact of removal: carried interest “haircut”?
- Additional Due Diligence on Economics and Control



Certain Issues Related to Private Equity Investments by Non-U.S. Investors

- Tax Issues
 - ECI / FIRPTA (income effectively connected with at US trade or business)
 - Overall reductions to investors due to tax / withholding issues
 - Filing of U.S. and Non-U.S. tax returns
- Foreign Corrupt Practices Act
- SEC-registered investment advisers
- Local Regulatory Constraints on Alternative Investments



Other Issues

- Co-investments and governance issues for minority investors
- Local tax issues and structuring
- Role of counsel for the institutional investor
- Private equity vs. venture capital structure and terms
- Fund-level leverage



Q&A

- QUESTIONS???



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- **Proskauer's Private Investment Funds Group** is comprised of over 100 professionals in offices in major business centers worldwide, including Boston, New York, London, Los Angeles, Paris, Hong Kong and São Paulo. The group counsels more than 100 U.S. and non-U.S. institutional investors in their alternative investment programs, including **fund investments**, **co-investments**, **managed accounts**, **secondaries** and **customized investment solutions**.
- Our lawyers advise on investments that span the alternative asset class on a daily basis, and our clients benefit from the industry knowledge this brings to bear on their projects. We have extensive familiarity with the terms, concepts, language and conditions found in typical investment fund and co-investment agreements, having written, reviewed and negotiated such documents for both sponsors and investors. Our knowledge of current terms and conditions is unparalleled and allows us to play a leading role in negotiations concerning both business and legal issues. In addition, we closely follow legal and marketplace developments, including tax law changes and accounting and regulatory developments, as well as advising our clients globally on their portfolio asset allocation and other strategic issues. Our institutional investor clients include:
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- We work with our clients to identify the legal and business risk in prospective portfolio investments, and provide practical, business-focused advice. We strive to provide best-in-class service, and our integrated team approach allows clients to draw upon the skills and experience of lawyers across all of the Firm's practices and offices.
- From 2007-2010 we negotiated and closed **over 1,280 investments representing \$46.5 billion dollars** across the alternative asset class.
- *Chambers Global* noted, the lawyers in the group are well-known in the industry as "**specialists who can always home in on the defining issues.**"



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