

Summer 2010

Editor's Note

As foreshadowed in our Spring Newsletter, we have continued to see momentum build in private equity deal-making over the last several months. In particular, we have seen competition for attractive target companies heat up as private equity buyers faced with rapidly approaching investing deadlines look for attractive investment opportunities. The loosening of the credit markets has added fuel to this activity; however, buyers will still need to put up a significant equity stake as lenders remain cautious in the amount of leverage they will allow. Perhaps most encouraging is the fact that private equity deals are taking many different forms – ranging from early stage activity such as backing a management group to create a new platform company to deals between private equity firms and sales to strategic companies. In the background of this activity, limited partners continue to show an appetite for committing capital in a fundraising market in which private equity firms are willing to make concessions in order to attract investors. We expect that these trends will continue to evolve in the coming months and will continue to keep you posted as they do.

Dominick DeChiara
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Practical Effect Of Dodd-Frank On Private Equity Funds

President Obama signed into law, on July 21, 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act. It is a mind-numbing 2,319 pages (Glass-Steagall was only 35), and there are an almost incomprehensible number of studies (67), rules and regulations (243), which multiple federal agencies are required to undertake in order to implement the legislation¹. For that reason, much of the effectiveness is delayed and uncertain in detail, but we wanted to alert private equity fund manager and investor clients of the two most practical and direct implications for private equity funds.

Registration Of Fund Managers Under Investment Advisers Act of 1940

First, private equity fund managers (not the funds) will have to register with the SEC as investment advisers, pursuant to the Investment Advisers Act of 1940. Some of you are already registered; those who are not have likely been relying on an exemption from such registration for an adviser having less than 15 “clients,” each fund being one client. That so-called “Private Client” exemption will be eliminated effective July 21, 2011. There are exceptions to the new registration requirements, including an exemption for advisers to “venture capital funds,” which the SEC is required to define.

While most private equity fund advisers will be required to register, there is a chance that smaller or medium-sized buyout fund advisers will fit into a new exemption for advisers to venture capital funds, especially those that utilize insignificant amounts of leverage. As a regulatory policy matter such funds have more in common with “VC” funds than mega-buyout funds or hedge funds, so it is possible that the SEC will define “VC” broadly enough to pick up more than what is considered a traditional “VC” fund manager.

Registration as an investment adviser, while cumbersome, should not be viewed as “game-changing” regulation. Many fund managers are already registered. It will of course require some designated personnel to focus on compliance, increase required record keeping, and subject files and procedures to occasional SEC review. Even advisers that are exempt from registration may need to comply with additional record keeping which the SEC is expected to mandate.

Limitation of Bank Investment in PE Funds

Second, with respect to any “banking entity”² investor in a fund, fund managers should be concerned about such entity’s ability or desire to invest in future funds. Unless future regulations take a different tack, it appears a banking entity

¹ Dodd-Frank is the most sweeping financial regulation since the 1930s. In comparison, in response to events leading to the Great Depression and related events, the federal government adopted six different securities acts over a seven-year period:

- The Securities Act of 1933
- The Securities Exchange Act of 1934
- The Public Utilities Holding Company Act of 1935
- The Trust Indenture Act of 1939
- The Investment Company Act of 1940
- The Investment Advisers Act of 1940

In a more complex financial world, Dodd-Frank attempts to mandate broad sweeping changes in one fell swoop.

² A “banking entity” is defined to include not just a bank or thrift (an “insured depository institution”) but also its parent (and any firm that is treated as a bank holding company by the International Banking Act) and affiliates and subsidiaries of its parent. Thus, a bank-owned firm would be prohibited from investing in a private equity fund or “sponsoring” such a fund, unless the investment or sponsorship comes within certain “permitted activities”. Subject to the study by the Financial Stability Oversight Council, the Federal Reserve Board is also authorized to adopt rules and capital requirements for non-bank firms determined to be “systemically significant”.

will be prohibited from investing its own capital, or retaining investments, in any PE fund or hedge fund. A banking entity will be permitted to invest customer funds into third party PE and hedge funds, through, for instance, separate accounts and other managed accounts. Subject to certain conditions discussed below, a banking entity's investment of its own capital will be permitted in private funds the banking entity organizes and sponsors (referred to herein as "bank-sponsored funds"), up to three percent of that fund's commitments. In the aggregate, a banking entity's investments in all private funds it organizes and offers—PE, hedge, VC, real estate, etc.—must be limited to three percent of the banking entity's Tier 1 capital. On its face, Dodd-Frank appears to have the effect of also prohibiting investments by bank-sponsored funds in PE funds and hedge funds in that such bank-sponsored funds may be considered "affiliates" of a bank and, thus, constitute "banking entities" themselves. It is not clear that the legislation really intended to prohibit bank-sponsored funds from investing in PE funds or hedge funds, and this issue may be addressed after a mandated study has been completed and regulations are issued.

With respect to existing investments of bank capital in private funds, the phase-in period for the banks' compliance could be fairly generous, although detail regarding the time periods remains to be worked out in further regulations and is subject to much discretion by bank regulators. The phase-in for full compliance appears to be almost four years in total, with a banking entity having the possibility to receive, at the discretion of bank regulators, extensions of an additional three to eight years thereafter. As a practical matter, the phase-in may be deferred long enough so that the new limitations are not an issue for many existing funds.

The limitations are to take effect not immediately, but after a conformance period for divestiture and an extended transition period, on the earlier of (i) 12 months after the date of issuance of final rules by

the banking agencies, SEC, and CFTC, or (ii) two years after the date the President signed the bill (two years would expire July 21, 2012). The regulators are required to adopt rules within nine months after the newly-established Financial Stability Oversight Council completes a six-month study on implementing the limitation. This means that the effective date could be as early as October 21, 2011, but, given the number of federal agencies that need to participate in the study and ultimately adopt implementing rules and regulations, more likely July 21, 2012.

Existing investments that thereby became prohibited (i.e., not fall within permitted exceptions) would then have to be divested over a conformance period (two years, subject to three one-year extensions) and an extended transition period (one up-to-five-year extension) to the extent necessary to fulfill a contractual obligation in effect on May 1, 2010 to take or retain an ownership interest in, or otherwise provide additional capital to, an "illiquid fund", which includes private equity funds.

To the extent that a banking entity does not seek, or regulators do not grant, necessary extensions, banking entities may need to pursue options including secondary market sales or exercise of any applicable withdrawal rights provided in fund agreements. Other options to assist banking entities come into compliance could be explored, such as, in some cases, in-kind distributions. Unlike hedge funds, dilution down to three percent through new equity issuances or redemptions down to three percent are not realistic solutions for private equity funds.

Bank-sponsored Funds

The statute generally prohibits a banking entity from "sponsoring" a hedge fund or private equity fund, subject to certain "permitted activities". "Sponsoring" is defined to mean serving as a general partner, managing member, or trustee (or selecting

or controlling (or having employees or directors or agents who constitute) a majority of the directors, trustees, or management of a fund) or sharing a common name or variation thereof. Thus, a bank-owned firm generally would be prohibited from serving as a general partner of a fund, subject to “permitted activities.”

Notwithstanding the general prohibitions, the legislation expressly permits certain activities in order to permit banks to continue to provide investment advisory services to customers. Therefore, “permitted activities” includes organizing a private equity fund, including serving as a general partner, managing member, or trustee of the fund (and selecting or controlling (or having employees, directors, or agents who constitute) a majority of directors, trustees or management of the fund) if the following eight conditions are met:

- (1) the banking entity provides bona fide trust or investment advisory services;
- (2) the fund is organized and offered only in connection with the provision of such services only to customers of such services;
- (3) the banking entity does not, after one year after the fund’s establishment, hold more than a three percent ownership interest in the fund (in addition to an aggregate cap of all interests in funds not exceeding three percent of the banking entity’s Tier 1 capital);
- (4) the banking entity complies with prohibitions against any banking entity that manages, advises, or sponsors a fund extending credit to or on behalf of the fund, buying assets from the fund, taking fund shares as collateral for extensions of credit to any person, or engaging in derivatives, repo, or securities lending or borrowing transactions with the fund, and all transactions between the banking entity and the fund being non preferential;
- (5) the banking entity does not guarantee, assume, or insure the obligations or performance of the fund or of any fund in which the fund invests;
- (6) the banking entity does not share its name or a variation thereof with the fund;
- (7) no director or employee of the banking entity, other than a director or employee directly engaged in providing services to the fund, takes an ownership interest in the fund; and
- (8) the banking entity discloses to prospective and actual investors in writing that losses in the fund are borne solely by the investors and not by the banking entity.

Thus, these are the circumstances under which a banking entity may sponsor or acquire an ownership interest in a fund. Where these circumstances exist, a bank-owned firm can serve as a general partner in a fund. We expect forthcoming rules and regulations to further define these conditions, particularly number (2) above.

Summary

The enormity of the financial regulation envisioned by this legislation cannot be overstated. The Financial Stability Oversight Council study to be undertaken by the various federal agencies, and then the rules and regulations to be adopted and coordinated among the banking agencies, the SEC, and the CFTC, are mind-numbing. Many of you may have questions and concerns as to your specific circumstances; we recommend you consider bringing your concerns to the attention of the regulators so that ambiguities, contradictions and unnecessary disruptions are minimized or at least addressed in advance.

We are happy to discuss any questions, issues or specific circumstances.

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Proposed Legislation to Tax Carried Interests as Ordinary Income

On May 28, 2010, the House of Representatives passed the American Jobs and Closing Tax Loopholes Act of 2010, H.R. 4213, which included a long-expected provision that generally would tax a portion of the income and gains associated with carried interests as ordinary income and net earnings from self-employment, regardless of the character of the income at the partnership level. In addition, on June 8, 2010, the Senate unveiled its initial version of H.R. 4213 that closely tracked the House bill but softened some of the carried interest provisions. As of July 16, 2010, Senate Finance Committee Chair Max Baucus (D-Mont.) had tabled H.R. 4213 after three failed attempts to advance the bill, each of which included a revised carried interest provision.

It is currently unclear whether the Senate will revisit H.R. 4213 in the near future. However, it is possible that H.R. 4213 will be revisited or the carried interest provisions will be included in another bill.

Background. In most private equity funds, managers' carried interests are structured as interests in the underlying fund partnership. Carried interests generally represent a sharing of profits (e.g., 20%) beyond a predetermined hurdle or a sharing of profits based on "waived fees." Under current law, a partner's distributive share of each item of partnership income, gain, loss, deduction and credit (including long-term capital gain) retains its character when allocated to the partner. Accordingly, when a partnership recognizes long-term capital gain (or qualified dividend income), the partners in such partnership pay tax at the favorable capital gains rate (currently 15%) rather than the ordinary income rate (currently 35%). Consequently, under current law, a significant portion of the income recognized by private equity fund managers in respect of their carried interests is treated as long-term capital gain rather than ordinary income.

"The House-approved bill and recent Senate bill would both change the law with respect to carried interest"

Overview of Proposals. The House-approved bill and the most recent Senate bill would both change the law with respect to carried interests. Specifically, the bills generally characterize a portion of net income allocated to a partner with respect to a carried interest as ordinary income and net earnings from self-employment, regardless of the character of the income at the partnership level. In addition, both bills characterize gain on the sale of a carried interest as ordinary and net earnings from self-employment. Finally, both bills treat any built-in gain with respect to appreciated property distributed in kind to a carried interest holder as an increase in such partner's current distributive share of partnership income and therefore subject to ordinary income treatment at the time of such distribution. Both bills would treat a portion of losses in respect of carried interests as ordinary losses up to the amount previously treated as ordinary income.

Self-Employment Tax. Income treated as ordinary under both the House and Senate bills would also be treated as net earnings from self-employment and therefore subject to the uncapped Medicare tax of 2.9% in 2011 and 2012. Beginning in 2013, however, the Medicare tax rate is scheduled to increase to 3.8% and will also apply to the net investment income of certain high-income taxpayers. Therefore, starting in 2013, the Medicare tax of 3.8% will generally apply to any income in respect of a carried interest, whether or not treated as ordinary income.

Applicable Percentages. The House bill provides that in the case of an individual, only 50% of net income or net loss in respect of a carried interest will be treated as ordinary income in 2011 and 2012. For taxable years beginning in 2013, however, the

House-approved bill would treat 75% of such income as ordinary income. In contrast, the latest Senate bill would treat 75% of carried interest net income as ordinary income starting in 2011. The Senate bill, however, includes an additional provision for a 50/50 split between ordinary and capital gain treatment for income attributable to the sale or exchange of any asset which is held at least five years. Under the Senate bill, this lower 50% recharacterization percentage also applies to the gain or loss attributable to the underlying partnership assets when a carried interest is sold. The portion of carried interest net income not treated as ordinary income under the proposed bills would continue to be treated as a distributive share of the underlying partnership's income (and taxed based on its underlying character). For taxpayers other than individuals (such as corporations and certain trusts), however, 100% of income with respect to a carried interest would be treated as ordinary income starting in 2011.

Based on the current bills, the effective tax rates on carried interests held by individuals beginning in 2011 (as compared to current law scheduled to be in effect) would be as follows:

	Current Law	House Bill	Senate Bill	Senate Bill (Assets Held 5 Yrs.)
Tax Rate on Carried Interests in 2011-2012	20.0% (includes capital gains rate increase to 20% in 2011)	31.25% (includes 50% of 2.9% Medicare tax)	36.875% (includes 75% of 2.9% Medicare tax)	31.25% (includes 50% of 2.9% Medicare tax)
Tax Rate on Carried Interests in 2013	23.8% (includes 3.8% Medicare tax)	38.5% (includes 3.8% Medicare tax)	38.5% (includes 3.8% Medicare tax)	33.6% (includes 3.8% Medicare tax)

Investment Services Partnership Interests. Both the House-approved and latest Senate bills would only apply to investment services partnership interests ("ISPIs"). The bills define an ISPI as any interest in a partnership held (directly or indirectly) by any person if it was reasonably expected at the time of acquisition of such interest that such person

(or a related person) would provide a substantial quantity of investment management services with respect to the partnership's "specified assets." Most, if not all, carried interests held by private equity fund managers would be treated as ISPIs.

Qualified Capital Interests. Neither the House nor the Senate's proposals would apply to allocations in respect of or dispositions of any portion of an ISPI that is a "qualified capital interest" so long as allocations to the qualified capital interest are made in the same manner as significant allocations made to capital interests held by non-service providers. Allocations to a private equity fund manager's interest will not be treated as being made in a different manner as allocations to other partners' qualified capital interests (*i.e.*, the limited partners) merely because of a failure to self-charge "carry" or management fees.

A "qualified capital interest" is generally defined as the portion of a partner's interest attributable to contributions of cash or property by the partner, allocations of taxable income to the partner, and any taxable income recognized by the partner as a result of such partner's initial receipt of such interest. An

interest will not be a qualified capital interest to the extent such interest is acquired with the proceeds of any loan or other advance made or guaranteed, directly or indirectly, by any other partner or

the partnership (or a person related to such partner or partnership). Carried interests generally would not constitute qualified capital interests.

Anti-Avoidance Provisions. Both the House and Senate proposals include provisions directed at preventing fund managers from avoiding the

new rules by holding interests designed to achieve economic returns similar to a carried interest in a partnership. Accordingly, interests in foreign corporations not subject to U.S. tax, convertible or contingent debt or options, certain derivative contracts, and certain other arrangements, would be treated as “disqualified interests” and subject to rules similar to those applicable to carried interests.

Increased Penalty. Both the House and Senate bills include an increased 40% understatement penalty (double the usual 20% penalty for understatements). Further, taxpayers would not be able to obtain reasonable cause relief to avoid the penalty, although with disclosure, the penalty could be avoided as long as the taxpayer had substantial authority and believed its position was more likely than not correct.

Effective Date. Both the House and Senate bills would be effective starting January 1, 2011. Accordingly, the rules above would not apply to appreciated property distributed in kind or the sale of a carried interest occurring on or before December 31, 2010. The new rules would also not apply to long-term capital gain or qualified dividend income attributable to a carried interest that is recognized with respect to a portfolio company on or before December 31, 2010.

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The Rise of Venture Debt in Europe: BCVA Report

In May 2010, Barry Vitou, a partner in our London office, sponsored the publication of the British Venture Capital Association’s (“BVCA”) report on “The Rise of Venture Debt in Europe”. The BCVA is the leading industry body and public policy advocate for the private equity and venture capital industries in the UK. The report is the first to capture the overall size of the venture debt industry across Europe and was presented to a packed audience of BVCA

members at our London office to raise awareness among the UK and European private equity industry of the availability and use of venture debt.

“... venture lenders are very much open for business and looking for new deals in 2010”

Venture debt has been around since the 1960s in the U.S., but is a more recent phenomenon in Europe. The European venture debt industry officially launched in 1998 with the arrival of European Venture Partners (now Kreos Capital). Since then, a bevy of other venture debt providers have emerged on the scene, including Silicon Valley Bank which entered the EU in 2005 and whose investments now equal approximately US\$1.5 billion across the EU.

The report provides detailed facts and statistics about an industry in Europe for which public data normally is not easy to obtain. Of the many interesting facts to emerge, the report revealed:

- Close to 400 companies have received venture debt from UK venture lenders with over US\$600 million invested in UK companies, over US\$600 million in European companies and over US\$300 million in companies in the rest of the world (mostly in Israel);
- Companies in the internet, biotech and semiconductor sectors had the highest average loan size (US\$5 million); and
- Half of the VCs that responded to the survey sent out by the BVCA indicated that up to 40% of their portfolios use venture debt.

The launch event included a panel discussion chaired by Barry Vitou and a representative from each of the BVCA and three leading venture debt providers, namely ETV Capital, Kreos Capital and Noble Venture Finance. The panel dispelled some of the myths surrounding the venture debt industry and, on a promising note, concluded that after the

economic turbulence of 2009 during which activity in the venture debt market slowed (and mirrored the situation in the private equity market), venture lenders are very much open for business and looking for new deals in 2010.

Copies of the report are available by clicking [here](#) or by requesting a copy from Barry Vitou (bvitou@winston.com). Our London office has a vibrant Emerging Growth company Venture Capital and Private Equity practice and is a recommended firm in the Legal 500 for Venture Capital and recognized as team which “*knows its tech inside out and targets start-up companies in the digital, new media, and emerging technology fields*”.

Barry Vitou, Partner

Elimination or Waiver of Fiduciary Duties in DE Fund Agreements

Delaware’s freedom of contract principles, evolving statutes and business acumen within its court system have clearly made it the state of choice for entity organization, including most private equity funds, such that approximately 600,000 limited liability companies and limited partnerships are organized in Delaware. The Delaware legislature expressly authorized the elimination of fiduciary duties in the limited partnership and limited liability company context in 2004.¹

In September of 2009, the Institutional Limited Partner Association (the “ILPA”), a non-profit

association committed to serving limited partner investors in the global private equity industry, issued its set of Private Equity Principles (the “Principles”) intended to restore and strengthen the basic alignment of interests between investors and fund sponsors. The Principles are ILPA’s suggested best practices that speak to issues relating to the alignment of interests, fund governance and transparency and reporting. Included within the best practices for fund governance is a reaction to a mini-trend among some sponsors disclaiming any fiduciary duty to limited partners. This minority trend and the ILPA position to the contrary is causing practitioners to refocus on the tension between the ability of a private equity sponsor’s ability under Delaware law to contract away fiduciary duties and that same private equity sponsor’s fiduciary duty under Section 206 of the Investment Advisers Act of 1940, as amended (the “Advisers Act”).

Delaware Acts

By way of background, prior to 2004, the Delaware Revised Uniform Limited Partner Act, 6 Del. C. §§ 17-101, *et seq.* (“DRULPA”) and the Delaware Limited Liability Company Act, 6 Del. C. §§ 18-101, *et seq.* (“DLLCA”, and together with DRULPA, the “Delaware Acts”) provided for the “restriction” of fiduciary duties but did not expressly provide that such duties could be “eliminated” in their entirety.² While the Chancery Courts found on many occasions in the limited partnership context that such duties could be eliminated, the Delaware Supreme Court took an opposing view, noting that DRULPA

¹ The Delaware Revised Uniform Limited Partner Act provides that “[t]o the extent that, at law or in equity, a partner or other person has duties (including fiduciary duties) to a limited partnership or to another partner or to another person that is a party to or is otherwise bound by a partnership agreement, the partner’s or other person’s duties may be expanded or restricted or eliminated by provisions in the partnership agreement; provided that the partnership agreement may not eliminate the implied contractual covenant of good faith and fair dealing.” The Delaware Limited Liability Company Act provides the same ability.

² Andrew S. Gold, *On the Elimination of Fiduciary Duties: A Theory of Good Faith for Unincorporated Firms*, 41 Wake Forest L. Rev. 123, 143 (2006).

did not authorize the elimination of a general partner's fiduciary duties.³ The passage of the 2004 amendments to the Delaware Acts specifically authorizing elimination of fiduciary duties came on the cusp of the private equity boom. With the newly amended express authorization, some private equity fund sponsors began to include provisions in their partnership agreements⁴ whereby their limited partners expressly agreed to eliminate or waive all fiduciary duties of the general partner.⁵ Such provisions eliminated the general partner's fiduciary duties of care and loyalty, duties that otherwise are implied by law.

Once fiduciary duties are eliminated or waived, the general partner is only subject to the implied contractual duties of good faith and fair dealing, which cannot be waived by statute, and which are contractual and not "fiduciary" duties in nature. This changes the traditional general partner-investor relationship from a fiduciary relationship to a contractual relationship, comparable to any non-fiduciary contract relationship between two commercial parties. If the partnership agreement provides for an elimination or waiver of fiduciary duties, the general partner is required to fulfill its express contractual undertakings but should not otherwise be required to generally act in the best interest of the partnership. So long as the general partner is not in breach of a specific contractual

undertaking, the limited partners should not have a cause of action (or more practically, the threat of or possibility of a legal action) were the general partner to engage in conduct to its benefit and to the detriment of the partnership.

Advisers Act

Notwithstanding Delaware's broad freedom of contract principles, the Advisers Act may prohibit conduct which is seemingly permitted under the Delaware Acts. Section 206 of the Advisers Act ("Section 206") sets forth the antifraud provisions of the Advisers Act and applies to all investment advisors (whether or not registered⁶), including general partners of private equity funds. On its face, Section 206 makes it unlawful for an investment advisor to engage in fraudulent, deceptive or manipulative conduct. The Supreme Court has held that Section 206 not only prohibits fraudulent conduct but imposes a fiduciary duty on the investment advisor.⁷ The Securities and Exchange Commission (the "SEC") has taken the position in the "hedge clause" context that Section 206 is violated by the use of any legend, hedge clause or other provision which is likely to lead an investor to believe that it has in any way waived certain rights of action against the investment advisor that are non-waivable under relevant federal or state law. We are unaware of any case or SEC action directly

3 *Id.* See also *Sonet v. Timber Co.* 722, A.2d 319 (1998) and *Gotham Partners v. Hallwood Realty Partners*, 817 A.2d 160 (2002).

4 Partnership and limited liability company should be used interchangeably. Most private equity funds use a limited partnership entity but the concept applies equally to limited liability companies.

5 While the Delaware Acts permit the parties to contract out of the fiduciary duties of loyalty and care, they expressly disallow the ability to contract out of the implied contractual covenant of good faith and fair dealing.

6 Section 206 applies to advisors relying on an exemption from registration pursuant to Section 203(b) of the Advisers Act - the "less than 15 client" exemption relied upon by many private equity sponsors.

7 *SEC v. Capital Gains Bureau*, 375 U.S. 180 (1963) (defining an investment advisor's fiduciary duty as "an affirmative duty of utmost good faith, and full and fair disclosure of all material facts, as well as an affirmative obligation to employ reasonable care to avoid misleading [his or her] clients") and Thomas P. Lemke and Gerald T. Lins, *Securities Law Handbook Series: Regulation of Investment Advisors*, Thomas West (2008) (stating "the purpose of the duty is to eliminate conflicts of interest and to prevent an advisor from overreaching or taking unfair advantage of a client's trust"). See also *Transamerica Mortgage Advisors, Inc. v. Lewis*, 444 U.S. 11 (1979).

providing that an elimination or waiver of fiduciary duties under Delaware law is a violation of Section 206. However, in the hedge clause context, the SEC has stated that the Advisers Act prohibits contractual provisions that purport to waive compliance with the Advisers Act or the rules thereunder.⁸ Thus, despite being expressly authorized by the Delaware Acts, it would appear that an elimination or waiver of fiduciary duties could subject a general partner to an enforcement action by the SEC for a violation of Section 206.

“...it’s unlikely that the market pendulum for private equity fund partnership agreements will swing toward eliminating fiduciary duties”

Summary

Conceptually, the freedom of contract principle and the ability to eliminate or waive fiduciary duties may make sense in certain contractual arrangements effected through a partnership structure subject to the Delaware Acts (e.g., a 50/50 joint venture among competitors or certain disclosed conflicts of interests). Given the Principles, institutional investors will likely resist the elimination or waiver of fiduciary duties in private equity fund partnership agreements going forward. Such resistance, coupled with the lack of clarity in the SEC’s position as to how Section 206 duty applies to private equity fund sponsors, makes it unlikely that the market pendulum for private equity fund partnership agreements will swing toward eliminating fiduciary duties.

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⁸ Section 215(a) of the Advisers Act.

Private Equity Update
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Firm Overview

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