

## *Private equity through the SEC's lens*

An extract from  
Asset Management News  
June 2011

*Investors' view of value has become wider. Performance still comes first, but factors such as competitive fees, strong infrastructure and transparency matter more than ever.*

June 2011



# Private equity through the SEC's lens

*With regulation imminent for private equity firms with activities in the US, understanding the SEC's likely perspective on some established practices can only bolster the brand.*



**Brendan McMahon**

PwC (Jersey)  
+44 1534 838234  
brendan.mcmahon@je.pwc.com



**Elizabeth Theford**

PwC (UK)  
+44 20 7213 3931  
elizabeth.b.x.theford@uk.pwc.com

Private equity firms all over the world will soon need to see their activities through the lens of the US regulator, the Securities and Exchange Commission (SEC). And the SEC may well believe that what seemed perfectly respectable in the long era of self-regulation does not correspond with its view of acceptable behaviour.

With US endowments and other institutional US investors a major source of private equity capital, many firms around the globe will need to register with the SEC and comply with the Investment Advisers Act of 1940 by the first quarter of 2012. While many non-US advisers may be exempt from registration, these exemption rules are not yet final and many of the rules require increased transparency to the SEC and compliance with various aspects of the Act.

Moving from an unregulated to a regulated environment is a substantial challenge. Firms must appoint a competent chief compliance officer and give the officer appropriate resources. Additionally, the firm must implement effective compliance programmes, backed by policies, procedures, testing and records. Beyond building the compliance infrastructure, they need to review working practices established over many years.

The SEC has been improving its knowledge of private equity firm practices through training and recruiting industry specialists, so we expect it will view some practices as unacceptable, and therefore grounds for deficiency letters or enforcement actions.

Being thoroughly prepared for regulation by foreseeing the SEC's views can only boost a firm's standing, both with investors and other stakeholders. But failure to do so might lead to civil, or even criminal, compliance actions.

## Practices to review

We believe that private equity firms should look at their practices in the context of a number of regulatory issues. In particular, they should look for potential conflicts of interest and make sure they identify, mitigate and disclose them. Firms should scrutinise the following practices for conflicts of interest:

- **Successive funds.** Using newer funds to support older funds' investments leads to potential conflicts of interest between the funds.
- **Allocation of investments.** When several funds operate in a similar area, firms should disclose to investors how they make allocation decisions. Similarly, when two funds both own

part of a portfolio company, the firm should disclose the valuation method for the company. Cross trades between funds should be executed using previously disclosed policies and procedures.

- **Expenses.** Expenses born by funds should be plainly disclosed, and the firm should not charge any additional expenses to the funds. Where there are co-investors in deals, expenses should be fairly allocated across all investors, especially in the case of broken deals.

Identifying all possible sources of material non-public information in order to prevent insider trading is another potentially troublesome area. Due to the complexity of the private equity business, there may be a number of potential sources. A compliance programme should include regular training on identification and mitigation of this risk.

Finally, the SEC requires that advisers keep all information needed to substantiate performance claims. Because private equity firms often use internal rates of return from previous funds for marketing purposes, they might have to keep performance data for long periods of time.

## Preparing across the firm

When preparing for registration, private equity firms should be sure that they have re-evaluated all practices that might be judged non-compliant by the SEC. They also need to make employees across the firm aware of the implications of compliance.

Making sure that the whole firm behaves within the letter and spirit of regulations can only boost the brand. The SEC is not alone in its focus on controls – regulators and investors everywhere want to see strong compliance programmes and control environments. Having this infrastructure in place allows top management to focus on creating portfolio value.

# Global Asset Management contacts

*Asset Management News is produced by experts in their particular field to address important issues affecting the asset management industry. If you would like to discuss any aspect of this document, please speak to your usual contact at PwC or a member of our global or territory leadership team.*

## Global Asset Management Leadership Team



### **Barry Benjamin**

PwC (US)  
Global Leader, Asset Management  
+1 410 659 3400  
barry.p.benjamin@us.pwc.com



### **Kees Hage**

PwC (Luxembourg)  
Global Leader, Real Estate  
+352 49 48 48 2059  
kees.hage@lu.pwc.com



### **John Parkhouse**

PwC (Luxembourg)  
European, Middle East & Africa Leader,  
Asset Management  
+352 49 48 48 2133  
john.m.parkhouse@lu.pwc.com



### **Pars Purewal**

PwC (UK)  
UK Leader, Asset Management  
+44 20 7212 4738  
pars.s.purewal@uk.pwc.com



### **Brendan McMahon**

PwC (Channel Islands)  
Private Equity Leader,  
Global Asset Management  
+44 1534 838234  
brendan.mcmahon@je.pwc.com



### **Robert Grome**

PwC (Hong Kong)  
Asia Pacific Leader, Asset Management  
+852 2289 1133  
robert.grome@hk.pwc.com



### **Will Taggart**

PwC (US)  
Global Tax Leader, Asset Management  
+1 646 471 2780  
william.taggart@us.pwc.com



### **Mike Greenstein**

PwC (US)  
Global Leader,  
Alternative Investments  
+1 646 471 3070  
michael.s.greenstein@us.pwc.com

## **Territory Leaders**

### **Argentina**

Diego Sisto  
+54 11 4850 4715

### **Australia**

Andrew Wilson  
+61 2 8266 3337

### **Austria**

Thomas Strobach  
+43 1 501 88 3640

### **Bahamas**

Dawn Jones  
+1 242 302 5300

### **Belgium**

Emmanuèle Attout  
+32 2 710 40 21

### **Bermuda**

Andrew Brook  
+1 441 299 7126

### **Brazil**

João Manoel dos Santos  
+55 11 3674 2224

### **Canada**

Rajendra Kothari  
+1 416 869 8678

### **Cayman Islands**

Graeme Sunley  
+1 345 914 8642

### **Channel Islands**

Brendan McMahon  
+44 1534 838234

### **Chile**

Roberto Villanueva  
+56 2 940 0070

### **China**

Alex Wong  
+86 21 2323 3171

### **Cyprus**

Costas Mavrocordatos  
+357 22 555 202

### **Czech Republic**

Glen Lonie  
+420 2 51 152 619

### **Denmark**

Mikael Sørensen  
+45 39 45 9269

### **Finland**

Tuukka Lahkela  
+358 9 2280 1333

### **France**

Alain Le Barbanchon  
+33 1 5657 1084

### **Germany**

Peter Seethaler  
+49 69 9585 3436

### **Gibraltar**

Edgar Lavarello  
+350 200 73520

### **Greece**

Mary Psylla  
+30 210 6874 543

### **Hong Kong SAR**

Robert Grome  
+852 2289 1133

### **Hungary**

Arpad Balazs  
+36 1 461 9163

### **India**

Gautam Mehra  
+91 22 6689 1155

### **Ireland (Republic of)**

Damian Neylin  
+353 1 792 6551

### **Isle of Man**

Michael Simpson  
+44 1624 689 689

### **Italy**

Elisabetta Caldirola  
+39 2 778 5380

### **Japan**

Takeshi Shimizu  
+81 90 6515 1754

### **South Korea (Republic of)**

Jae-Hyeong Joo  
+82 2 709 0622

### **Luxembourg**

Didier Prime  
+352 49 48 48 2127

### **Malaysia**

Mohammad Faiz Azmi  
+60 3 2173 0867

### **Malta**

Joseph Camilleri  
+356 2564 7603

### **Mexico**

Jose Antonio Quesada  
+52 55 5263 6000

### **Netherlands**

Fred Gertsen  
+31 10 407 6614

### **New Zealand**

Paul Mersi  
+64 4 462 7272

### **Norway**

Geir Julsvoll  
+47 95 26 05 40

### **Pakistan**

Rashid Jafer  
+92 21 2424500

### **Poland**

Adam Celinski  
+48 22 523 4330

### **Portugal**

António Assis  
+351 213 599 000

### **Russia**

Richard Gregson  
+7 495 967 6327

### **Singapore**

Yeow Chee Keong  
+65 6236 7298

### **Slovakia**

Christiana Serugova  
+421 2 59 350 614

### **South Africa (Republic of)**

Pierre de Villiers  
+27 11 797 5368

### **Spain**

Enrique Fernandez Albarracin  
+34 91 568 4504

### **Sweden**

Susanne Sundvall  
+46 8 555 332 73

### **Switzerland**

Thomas Huber  
+41 58 792 2436

### **Taiwan**

James Huang  
+886 2 2729 6666

### **Thailand**

Anothai Leekitwattana  
+66 2 344 1100

### **United Kingdom**

Pars Purewal  
+44 20 7212 4738

### **United States of America**

Barry Benjamin  
+1 410 659 3400

If you would like to receive copies of this newsletter or would like further information about PwC's asset management publications, please contact [denise.cook@uk.pwc.com](mailto:denise.cook@uk.pwc.com)

Editor: Rupert Bruce

[www.pwc.com/assetmanagement](http://www.pwc.com/assetmanagement)

This publication has been prepared for general guidance on matters of interest only, and does not constitute professional advice. You should not act upon the information contained in this publication without obtaining specific professional advice. No representation or warranty (express or implied) is given as to the accuracy or completeness of the information contained in this publication, and, to the extent permitted by law, PricewaterhouseCoopers does not accept or assume any liability, responsibility or duty of care for any consequences of you or anyone else acting, or refraining to act, in reliance on the information contained in this publication or for any decision based on it.

© 2011 PwC. All rights reserved. Not for further distribution without the permission of PwC. "PwC" refers to the network of member firms of PricewaterhouseCoopers International Limited (PwCIL), or, as the context requires, individual member firms of the PwC network. Each member firm is a separate legal entity and does not act as agent of PwCIL or any other member firm. PwCIL does not provide any services to clients. PwCIL is not responsible or liable for the acts or omissions of any of its member firms nor can it control the exercise of their professional judgment or bind them in any way. No member firm is responsible or liable for the acts or omissions of any other member firm nor can it control the exercise of another member firm's professional judgment or bind another member firm or PwCIL in any way.