

Funds in Focus 2018: Private Investment Funds Annual Review Conference

Year-end Updates and What to Look
Out for in 2019 for Hedge Funds

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Year-end Updates and What to Look Out for in 2019 for Hedge Funds

Key Business Trends and New Investor Demands

Key Business Trends

- New Economic Terms:
 - “1 or 30”
 - Increased use of private equity-style terms (hurdle, incentive fee/allocation on realized gains only and/or over multiple year period).
- Separate Managed Accounts and Single Investor Vehicles
- Single Investment Vehicles/SPVs:
 - Co-investment, excess/overflow capacity, best idea, sidecar funds.
 - Investor-sponsored “best idea”/co-investment platforms.

New Investor Demands

- Add common side letter provisions to Fund documents, e.g.:
 - Notice of key developments (litigations, proceedings, etc.).
 - Use reasonable efforts to terminate any suspension, to pay distributions in cash, give prior notice of distributions in kind, etc.
- New common side letter requests
 - Manager and principals subject to same redemption notice and terms as investors.
 - Right to be offered co-investment opportunities.
 - No fees during suspension (that continues for 6 or 12 months) or on side pocket.
 - No negative consent process.
 - Define “in Manager/GP’s sole discretion” to consider only fund/investor best interests.
 - Reaffirm GP/Manager’s fiduciary status and obligations.
 - Require independent board of directors of limited partnerships/master funds.
 - ESG vehicles/classes.



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Top 5 Tax Takeaways

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1. Ready for it: The partnership tax audit rules are now effective.
2. Anything left: Incentive allocation planning.
3. Should I stay or should I go: Management company structuring issues.
4. Interested: Interest expense limitations.
5. Lose Control: Changes to the controlled foreign corporation rules.



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Key Regulatory and Litigation Risks

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- Privacy and Data Security Risks
 - The absence of a cybersecurity policy that includes emergency remedial measures may lead to regulatory scrutiny and possible enforcement action.
- Valuation
 - SEC likely to focus on issues around practices, consistency.
- Fund Performance Marketing
 - A continuing area of examination focus; proposed advertising rule.
- Conflicts
 - Have acts or practices that benefit the manager been sufficiently disclosed to investors?
- Big Data
 - Big risks: Privacy law breaches, insider trading, adverse publicity, agency liability, etc.

Key Regulatory and Litigation Risks

- Whistleblowers
 - Record bounties; retaliation policing.
- Pay-to-Play
 - Even small contributions (with no intent to influence) matter.
- Cryptocurrencies and ICOs
 - Prepare for regulatory scrutiny (and possible disputes if values collapse).
- Litigation Funding
 - Proliferation of new funds; likely secondary market.
- Enforcement Risks
 - Proactively identify and address potential violations before exam and consider engaging counsel.



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Year-End Tasks and Upcoming Regulatory Filings/Deliveries

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- Take a holistic view of all information available to investors – Do you have vertical integration?
- Consider preparing risk matrices for MNPI risks, cybersecurity risks, custody rule compliance, general compliance risks, side letter compliance, etc. (look at table of contents from your compliance manual).
- Training of employees on MNPI, cybersecurity, compliance manual (and/or specific sections where there have been prior issues), anti-harassment, etc.
- Take a recent SEC exam letter and gather documents and prepare responses.
- I trust you have been probing and testing all year.
- Annual Review – Written or not? Outline of what to do? Use outside consultant? Who hires them?
- Sit with senior management and make reports and recommendations.
- Insurance?
- Read our Annual Review.

Year-End Tasks and Upcoming Regulatory Filings/Deliveries

- Upcoming Filings/Deliveries
 - Form ADV Part 1 and Part 2A Updates – April 1st (for advisers with a December 31 fiscal year-end).
 - Form D and State Blue Sky Filings.
 - Form PF (March 1st for Large Hedge Fund Advisers).
 - Fund Document Updates (if there have been material changes).
 - Privacy Policy Updates (if there have been material changes).
 - New Issues Affirmations.
 - Schedule 13D/13G Filing.
 - Form 13F Filing and 13H Annual Amendments – February 14th .
 - CFTC Form CTA-PR (February 14th) and CFTC Form CPO-PQR (March 1st).
 - CFTC Rule 4.13(a)(3) (or 4.7) Exemption Reaffirmation – March 1st.
 - ERISA Section 408(b)(2) notice – send notice of any changes to any ERISA managed account client and any ERISA investor in any fund treated as plan assets under ERISA.

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