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Lecture 17: 4/14/04

Guests: John LeClaire and David Watson, Partners, Goodwin Procter

What is private equity?
Real estate, investing in hi-tech, natural resource funds.

- A person targets on a specific industry.
- What is a private equity fund?
  - Opt to form an entity and get a commitment from investors to give you money over time so that you can invest in companies.
- 1st step when a client comes to them: Do you look at the market?
  - Where are your businesspeople?
  - Put management team together
  - Do preliminary market track record.
- 2nd step:
  - structure fund
  - What kind of structure should you use?
    - What kind of partnership
    - When choosing you don't want to pay taxes at basis level
    - Capital gain vs. ordinary
    - Jurisdiction (Delaware is where you want to form an entity)
    - Put money for 8-10 years
    - NASD just passed a new rule on when you can invest in an IPO.
- 3rd rule: after structuring
  - What are the terms of the offering
  - Manager gets 80% of profits.
  - Investment period: 4-5 years (where you are putting the money to work)
  - Offsets: as a fund manager you don't' want to get a fee from the portfolio company.
  - 6-9 months is the time period when you can bring in investors
  - When you kick off fundraising you bring investors, and negotiate early-on.
    - Sign all the necessary documents to show "commitment"
  - Within 10 year time period you need to liquidate assets.
  - Carried interest: a share of the profits
    - How do you calculate it?
      - Usually calculated on a fund-wide basis.
  - Look at value of portfolio and see if its above a certain threshold
  - Clawbacks: if I gave you $ early then you have to give some of it back.
  - Will the investors get a preferred return?
    - Issues is the priority on the term of payment

- Clients make 1st mistake in raising money
- A typical private equity fund is about $200,000 in legal fees.
- April 14, 2000: bubble burst (people were skittish to put $ in)