King & Spalding

Checklist for Non-U.S. Fund Managers Making a Private Fund Offering in the U.S.

The United States represents a large source of potential capital that non-U.S. fund managers often find impossible to ignore. To assist non-U.S. fund managers, we have prepared a checklist that sets out key considerations for non-U.S. fund managers to consider before marketing in the U.S. These considerations include relevant securities laws, tax considerations, benefit plan investor regulations and commodity exchange laws. This checklist does not purport to be a comprehensive list of matters for consideration, but is meant to be a useful starting point for non-U.S. fund managers. This checklist deals only with the raising of capital from U.S. investors, and does not address the myriad issues raised by making investments into the U.S. The information contained in this checklist does not, and is not intended to, constitute legal advice. Instead, all information and content are for general informational purposes only and we do not accept any liability for error or omission. Please contact King & Spalding LLP for specialist legal advice in relation to specific circumstances.

SECURITIES LAW COMPLIANCE

1 Will the fund be offered only to persons reasonably believed to be “accredited investors”? As of the date of this checklist, accredited investors include, among others:

- Entities, not formed for the specific purpose of acquiring fund interests, with total assets in excess of US$5 million;
- Natural persons who have an individual income in excess of US$200,000 (or joint income with the person’s spouse in excess of US$300,000) in each of the two most recent years, and a reasonable expectation of reaching the same income level in the current year; and
- Natural persons with individual net worth, or joint net worth with that person’s spouse, in excess of US$1 million excluding the value of the primary residence of such natural person.

Explanation: Generally, an issuer that offers or sells its securities in the United States must register the offering of those securities under Section 5 of the U.S. Securities Act of 1933, as amended (the “Securities Act”) or must qualify for an exemption from such requirement. Registration is not practical for most private investment funds. Consequently, a private investment fund will typically seek to rely on the private placement exemption in Section 4(a)(2) of the Securities Act, and, in particular, the safe harbor set forth in Rule 506(b) of Regulation D of the Securities Act (“Regulation D”). The Rule 506(b) safe harbor permits an issuer to sell its securities to “accredited investors” only. Please note, however, that a private fund that relies on section 3(c)(7) U.S. Investment Company Act of 1940, as amended (the “Investment Company Act”) needs to ensure its investors meet the “qualified purchasers” test (with exceptions for knowledgeable employees) (see item 7). For completeness, a SEC registered investment adviser needs ensure the investors in a private fund advised by it meets the more stringent “qualified client” test if it wishes to charge incentive compensation (see item 12).

2 Will the fund manager refrain from "general solicitation" or "general advertising"?

Explanation: An offering under Rule 506(b) must not involve "general solicitation" or "general advertising". As a general rule, no public statements in any medium should be made with regards to an investment in the fund or to other information that would be of interest to prospective investors in the fund. Such information may include:

- The fund's name or a description of the fund;
- The fact that the fund manager is in the process of raising a fund or communications about the type of investors being targeted by the fund manager;
- Any of the terms of the fund offering; and
- The fund manager's prior track record or performance.

Not surprisingly, advertisements, articles, notices or other communications published in any newspaper, magazine, publicly available website, or similar media or broadcast over television or radio are likely to amount to general solicitation or general advertising. Statements to reporters (including for trade journals), statements on the fund manager's website (unless access is restricted) and statements made at investor or industry conferences could also be viewed as general solicitation or general advertising. If a fund manager makes statements that could be viewed as general solicitation or general advertising, the SEC could impose a "cooling-off period" with respect to U.S. investors, which would typically involve a moratorium on fund raising activity and fund closings for a certain period. For completeness, we note that the safe harbor in Rule 506(c) permits general solicitation or general advertising, but this safe harbor is less frequently used because it requires more invasive verification of the subscriber's accredited investor status and the private investment company exclusions under the Investment Company Act exclude any public offering of securities (see discussion at item 7).

3 Will reasonable care be taken to ascertain that an investor is not a person who has purchased fund interests with a view to the distribution of the fund interests? Typically a fund will take reasonable care by:

- providing written disclosures that the fund interests have not been registered and cannot be resold unless they are registered or unless an exemption from registration is available;
- referring to the applicable restrictions on transfer in the limited partnership agreement (or similar governing agreement); and
- making enquiry (e.g. in the subscription agreement) as to whether an investor is acquiring the fund interests for itself or to sell to others.

Explanation: Securities offered in reliance of the safe harbor in Rule 506(b) cannot be resold without registration under the Securities Act or an exemption under the Securities Act.

4

Has the fund conducted reasonable diligence to ensure its "covered persons" are not the subject of a "disqualification event" which could prevent the fund from relying on the safe harbor in Rule 506(b)?

Explanation: Pursuant to Rule 506(d), a fund is prevented from relying on Rule 506 if certain persons affiliated with the fund are subject to certain disqualifying events. A fund's "covered persons" involve members of its general partner, members of its management team, its placement agent and any beneficial owner of 20% or more of its voting securities, which can include larger investors. If the disqualification event occurred prior to September 23, 2013, the fund may be required to disclose the disqualifying event but is not necessarily barred from relying on Rule 506(b).

5

Has the fund filed a Form D no later than 15 days after the date of the first sale of the fund interests?

Explanation: All issuers relying on Rule 506 of Regulation D are required to file Form D electronically with the U.S. Securities and Exchange Commission (the "SEC"). Amendments of Form D must be made if there are any material changes or if the fund's offering lasts beyond the one-year anniversary of the initial filing.

6

Has the fund checked whether it needs to comply with state-based securities laws ("Blue Sky" laws)?

Explanation: In addition to the U.S. federal securities laws, a fund may have to comply with selected state securities laws which could require filings with state authorities depending on the jurisdictions in which the sale or solicitation of interests are made (which is typically the U.S. investors' principal place of business or residence).

7

Will the fund interests be held by no more than 100 beneficial owners or, in the alternative, are all of the investors "qualified purchasers"? As of the date of this publication, "qualified purchasers" include, among others:

- natural persons who own not less than US$5 million in "investments"; and
- entities that own and invest on a discretionary basis not less than US$25 million of investments.

Explanation: Generally, any issuer that is, or holds itself out as being, engaged primarily, or proposes to engage primarily, in the business of investing, reinvesting or trading in securities must register with the SEC as an "investment company" pursuant to the Investment Company Act unless an exclusion from registration applies. Most private funds avoid registration as an investment company by relying on one of two private investment company exclusions set forth in section 3(c)(1) or section 3(c)(7) of the Investment Company Act. If a fund chooses to rely on the exclusion set forth in section 3(c)(1) of the Investment Company Act, it must have no more than 100 beneficial owners of its securities (not counting knowledgeable employees) and is not making, or proposing to make, any public offering of its securities. Under this exclusion, complicated "look-through" rules for purposes of determining beneficial ownership apply, such that the number of beneficial owners for the purposes of section 3(c)(1) is often higher than the number of direct investors in the fund. In addition, similar funds with the same fund manager may be viewed as a single fund for the purposes of the 100 beneficial owner limit, although a fund relying on section 3(c)(1) will not be integrated or combined with a fund relying on section 3(c)(7).

If a fund chooses to rely on the exclusion set forth in section 3(c)(7) of the Investment Company Act, all of the fund interests must be beneficially owned only by persons who, at the time of acquisition of the fund interests, are "qualified purchasers" or "knowledgeable employees". Further, the fund must not make, or propose to make, any public offering of its securities. A section 3(c)(7) fund may have an unlimited number of investors who are qualified purchasers (subject to a separate 1,999 investor limitation under the Exchange Act).

It should be noted that a non-U.S. fund need not count non-U.S. beneficial owners for the purposes of section 3(c)(1) or ensure non-U.S. investors satisfy the qualified purchaser requirements for the purposes of section 3(c)(7), as applicable. A non-U.S. fund relying on either private investment company exclusion is only prevented from making a public offering in the U.S.; in other words, such a fund may conduct public offerings of its securities outside the U.S. In contrast, a fund established in the U.S. must count all investors. Certain "knowledgeable employees" are excluded from the 100 beneficial owner count for the purposes of section 3(c)(1) and the qualified purchaser requirement set forth in section 3(c)(7). Such knowledgeable employees would include executive officers and certain participating employees of the fund or the fund manager. The requirements of section 3(c)(1) and section 3(c)(7) are ongoing requirements that must be complied with over the life of the fund, thus necessitating restrictions on any future sale or assignment of fund interests.

8 Unless the fund manager is a registered investment adviser, does the fund manager satisfy the requirements of the "foreign private adviser exemption"? In other words, does the fund manager:

- have no place of business in the U.S.;
- have, in total, fewer than 15 U.S. clients and U.S. investors in private funds advised by the fund manager;
- have aggregate assets under management ("AUM") attributable to these U.S. clients and U.S. investors in private funds advised by the adviser of less than $25 million;
- refrain from holding itself out generally to the public in the U.S. as an investment adviser; and
- not act as an investment adviser to any U.S. registered investment companies or U.S. business development companies.

If no, the fund manager must rely on another exemption from registration with the SEC or register as an investment adviser. Please go to item 9 .

If yes, the fund manager may rely on the "foreign private adviser exemption". Please skip to item 13 .

Explanation: The US Investment Advisers Act of 1940, as amended (the Advisers Act), generally regulates "investment advisers" that are based in the United States or who advise clients in the United States. Generally, any person who, for compensation, engages in the business of advising others as to the value of securities or to the advisability of investing in, purchasing or selling securities is subject to regulation as an "investment adviser" under the U.S. Investment Advisers Act of 1940, as amended (the "Advisers Act"). A fund manager that conducts fundraising activities in the U.S. will be required to register with the SEC as an investment adviser unless an appropriate exemption from registration applies. A fund manager relying on the "foreign private adviser" exemption under sections 202(a)(3) and 203(b)(3) of the Advisers Act, unlike the private fund adviser exemption and the venture capital fund adviser exemption, will not be considered an "exempt investment adviser" and subject to the obligations of an exempt reporting adviser (see discussion of these exemptions below).

9 Does the fund manager satisfy the below requirements of the "private fund adviser exemption":

- the fund manager's clients that are U.S. persons are all qualifying private funds, which includes private funds that rely on section 3(c)(1) or section 3(c)(7) of the Investment Company Act; and
- all assets managed by the fund manager at any U.S. place of business are solely attributable to private fund assets, the value of which is less than $150 million and the fund manager's principal place of business is outside the U.S.

If no, the fund manager must rely on another exemption from registration with the SEC or register as an investment adviser. Please go to item 10.

If yes, please skip to item 11.

Explanation: The exemption from registration can be found in section 203(m) of the Advisers Act. The above analysis assumes that the fund manager's principal place of business is outside the U.S. If the fund manager's principal place of business is in the U.S., all assets managed for U.S. and non-U.S. clients will be counted towards the $150 million threshold. Unlike the "foreign private adviser" exemption, there is no limit on the number of fund investors and the fund manager can maintain a place of business in the U.S. However, a fund manager relying on this exemption might not be able to advise U.S. clients that are single investor accounts or "fund of one" investment vehicles. Further, a fund manager relying on this exemption will be subject to the modified filing and recordkeeping obligations of an exempt reporting adviser (see below obligations of an exempt reporting adviser). The fund manager is required to calculate the fair market value of assets under management in the U.S. annually and will be required to register as an investment adviser within three months if it reaches or exceeds the $150 million threshold.

10 Is the fund manager an investment adviser only to "venture capital funds"? A "venture capital fund" is defined as a private investment fund that:

- represents to its investors and prospective investors that it carries out a venture capital strategy;
- holds no more than 20% of the fund's capital commitments in "non-qualifying investments" (other than short-term holdings). "Qualifying investments" typically consist of equity securities of "qualifying portfolio companies" that are generally directly acquired by the fund (and not on the secondary market);
- does not incur leverage or provide guarantees in excess of 15% of the fund's capital requirements, which borrowing, guarantee or leverage is on a short-term basis only (i.e. for a non-renewable term of no longer than 120 days);
- does not offer investors redemption, withdrawal or other similar liquidity rights except in extraordinary circumstances such as for regulatory reasons; and
- is not registered under the Investment Company Act and has not elected to be treated as a business development company.

If no, the fund manager may be required to register with the SEC as an investment adviser. Please skip to item 12.

If yes, please go to item 11.

Explanation: The rules allow the investment adviser to advise a fund that holds non-qualifying investments of up to 20% even if it makes other types of investments such as bridge loans, publicly offered securities and interests in other venture capital funds. The private fund adviser exemption, venture capital fund adviser exemption and foreign private adviser exemption are the exemptions from the Investment Advisers Act that are most commonly relied upon by non-US fund managers, but there are other exemptions including exemptions for small business investment companies, intrastate advisers and family offices. A fund manager that relies on the private fund adviser exemption or the venture capital fund adviser exemption is nevertheless subject to the modified reporting obligations of an "exempt reporting adviser" (commonly known as an "ERA").

11 If the fund manager relies on the private fund adviser exemption or the venture capital fund adviser exemption, has the fund manager complied with the requirements applicable to exempt reporting advisers including filing of an abridged Form ADV?

Explanation: An exempt reporting adviser is required to comply with a subset of the obligations applicable to SEC registered investment advisers pursuant to section 204(5) of the Advisers Act. One such obligation is the obligation to submit a shortened version of Form ADV to the SEC, which will be made publicly available on the SEC website. On Form ADV, the exempt reporting adviser will be required to identify that the exemption from investment adviser registration that it relies on. A Form ADV must be submitted within 60 days of relying on the exemption and then at least once annually within 90 days of an adviser's fiscal year end. While an exempt reporting adviser is not expected to be subject to SEC examinations on a regular basis, unlike registered investment advisers, the SEC has the authority to conduct examinations.

12 Is the fund manager required to register with the SEC as an investment adviser and if so, has the fund manager complied with the requirements applicable to a SEC registered investment adviser?

Explanation: An investment adviser that does not qualify for any exemption from registration will be required to register with the SEC and comply with obligations under the Investment Advisers Act, including the following:

- Form ADV: A registered investment adviser will be required to submit Form ADV to the SEC on registration and at least once annually. Part 1 of Form ADV requires the investment adviser to include details of its business, ownership structure, relevant business practices, current and occasionally historical clients, key employees, and disciplinary events. Part 2 of Form ADV (also known as the "brochure") requires the investment adviser to provide disclosure of, without limitation, the advisory services offered, fees and expenses, investment fees, investment strategies, analysis methods, material risk factors, conflicts of interest, and key employees and management, pursuant to section 204(3) of the Advisers Act. Parts 1A and 2A of Form ADV are publicly available, while Parts 2A and 2B are typically delivered to fund investors.
- Form PF: A registered investment adviser will be required to submit Form PF, which is designed to allow the Financial Stability Oversight Council assess system risk related to private funds. The information that is required and frequency of reporting will depend on the type of fund (hedge fund, money market fund or private equity fund) and the quantum of assets under management.
- Restrictions on Incentive Compensation: A registered investment adviser may not charge incentive compensation (i.e. performance fees and carried interest) for a fund that it advises unless the investors in the fund meet a "qualified client" test (see item 12).
- SEC Examinations: A registered investment adviser can usually expect an examination of its books and records by the SEC before the first anniversary of its registration. The frequency of examinations thereafter will depend on the firm's risk profile.
- Other Requirements: A registered investment adviser must also comply with requirements related to record keeping, compliance programs, a code of ethics and custody.

TAX CONSIDERATIONS

13 Will the fund have U.S. taxable investors, U.S. tax-exempt investors or both? Has the optimal tax structuring of the fund been considered and does the fund documentation include necessary U.S. tax provisions?

Explanation: U.S. taxable investors and U.S. tax-exempt investors have very different tax profiles, and consequently it is important to consider fund structures suitable to the type of U.S. investor targeted. Even if the fund is structured in a jurisdiction where there is no income tax imposed at the fund vehicle level, the classification of the fund vehicle for U.S. federal income tax purposes would change the tax consequences for U.S. investors.

Generally, U.S. taxable investors prefer investment fund vehicles that are treated as partnerships for U.S. income tax purposes. Such vehicles receive "pass-through" tax treatment, which means that the fund vehicle itself will not be subject to U.S. federal income tax. Investment in entities treated as corporations for U.S. federal income tax purposes may result in unfavorable tax treatment for U.S. taxable investors. For example, investments in non-U.S. entities treated as passive foreign investment companies (commonly referred to as "PFICs") or controlled foreign corporations are subject to special tax rules. Any portion of such fund's income that is effectively connected with a U.S. trade or business would be taxed at the applicable U.S. federal income tax rate for corporation, which would result in the fund's income being subject to an additional layer of U.S. federal income tax.

In contrast, U.S. tax-exempt investors generally prefer in investment fund vehicles that is treated as a corporation for U.S. tax purposes. U.S. tax-exempt investors include pension funds, charities, university endowments and private foundations. A U.S. investor that is otherwise exempt from U.S. federal income tax may be subject to U.S. federal income tax liability if it recognizes "unrelated business taxable income" ("UBTI"). UBTI is income derived from a trade or business regularly carried on by a US tax-exempt entity that is unrelated to its exempt purpose. UBTI can be generated outside of the United States, such that UBTI considerations remain relevant for non-US funds with US tax-exempt investors. Key sources of UBTI include: (a) operating income from operating assets (which may be within or outside the U.S.) that are held in an entity that is treated as a partnership (i.e. a flow-through entity) for US federal income tax purposes; (b) the fund incurring debt that is allocated to its acquisition of an investment which may result in the income or gain attributed to such debt-financed investment may be treated as UBTI; and (c) management fee offsets resulting from monitoring, transaction and similar fees which may be treated as engaging in a trade or business and result in UBTI. U.S. tax-exempt investors vary in their tolerance of UBTI; while some prefer not to incur UBTI at all while for others it only form part of their assessment of the fund investment. It is possible for a fund to use "blockers", which is a commonly used term for an entity that is treated as a corporation for U.S. federal income tax purposes. Interposing a blocker does not eliminate the tax payment or tax filing obligation but instead places the burden of paying any applicable U.S. taxes and filing any applicable US tax returns on the blocker. The decision on whether or not to use blockers may depend on the administration and cost of such structures on the fund manager.

In addition, the fund manager should check if the fund documentation includes any necessary tax accounting provisions such as provisions dealing with the maintenance of capital accounts and provisions that provide how income and loss is allocated for US income tax purposes.

ERISA CONSIDERATIONS

14

Is the fund offered to U.S. pension plans or other investors that may be subject to the U.S. Employee Retirement Income Security Act of 1974 ("ERISA") or similar regulations? If yes, does the fund qualify for one of the exemptions from ERISA and ERISA-like regulations?

Explanation: A private investment fund typically seeks to ensure that its assets are not characterized as "plan assets" for ERISA purposes, since the consequences are severely restrictive. Plan asset status would result in the fund's investments being treated as the assets of the benefit plan investor, which would result in the fund, its manager and the general partner being subject to burdensome regulations and compliance requirements including but not limited to the imposition of fiduciary duties and constraints on fee arrangements. Although government pension plans are not technically subject to ERISA, many such plans are subject to ERISA-like regulations pursuant to state legislation.

Funds would typically rely on the so-called "under 25% exception" or the exemptions applicable to venture capital operating companies ("VCOC") or real estate operating companies ("REOC"). Under the "under 25% exception" exemption, benefit plan investors as a group (which includes U.S. private pension plans but excludes U.S. government plans or non-U.S. corporate plans) must constitute less than 25% of each class of interests in the fund. Any investments held by the fund manager, the general partner and their respective affiliates are excluded from both the numerator and denominator of the calculation for this purpose.

Alternatively, some funds may be able to rely on the VCOC exemption or the REOC exemption. While the under 25% exception can be relatively straightforward, complying with the VCOC exemption or REOC exemption typically involves careful planning. In essence, the fund must do the following: (a) obtain "management rights" with respect to at least 50% or more of its portfolio investments (based on cost); and (b) exercise those rights in the ordinary course of its business with respect to at least one portfolio company at the times specified in the regulations. To qualify at all, management rights must be obtained with respect to the fund's first portfolio investment. The portfolio companies must be operating companies engaged in the production or sale of a product or service other than the investment of capital. The REOC exemption is similar to the VCOC exemption, except that it is applicable to real estate funds.

COMMODITY EXCHANGE ACT CONSIDERATIONS

15

Does the fund trade commodity interests? If yes, is the fund able to rely on one of the exemptions from registration with the U.S. Commodities Futures Trading ("CFTC") as a commodity pool operator ("CPO") and a commodity trading adviser ("CTA")?

Explanation: A fund manager or general partner that manages or advises funds that trade in commodity interests (including future contracts, options on futures and swaps) may be subject to regulation under the U.S. Commodity Exchange Act, regardless of whether trading commodity interests forms part of the fund's investment strategy or is merely used to hedge portfolio risks or interest rate or foreign exchange exposure. It is typical for non-U.S. fund managers to rely on one of the exemptions from registration as a CPO, and the most commonly used exemption is the so-called "de-minimis exemption" available under CFTC Rule 4.13(a)(3).

To rely on this exemption:

A. The commodity pool only engages in a limited amount of trading in commodity interests, based on either of the following tests:

   (i) 5% test: the aggregate initial margin, premiums and required minimum security deposit required to establish such commodity interest positions does not exceed 5% of the liquidation value of the commodity pool's portfolio, after taking into account unrealized profits and unrealized losses on any such positions.

   (ii) net notional test: the aggregate net notional value of the pool's commodity interest positions (determined at the time the most recent position was established) does not exceed 100% of the liquidation value of the commodity pool's portfolio, after taking into account unrealized profits and unrealized losses on any such positions.

B. Participation in the pool is limited to certain types of qualified investors.

C. The interests in the commodity pool must be exempt from registration under the Securities Act and not publicly marketed in the United States.

D. The pool is not marketed as or in a vehicle for trading in the Commodity Interest markets.

Fund managers relying upon this registration exemption must (i) make certain disclosures to prospective participants regarding such exemption; (ii) file notice of such exemption with the National Futures Association ("NFA") with respect to each commodity pool for which it is claiming the exemption; and (iii) renew such exemptive filing on an annual basis.

There are a number of exemptions from registration as a CTA. One of the most commonly used, being CFTC Rule 4.14(a)(5), exempts a person from the requirement to register with the CFTC as a CTA if each of the following conditions is met:

- The person is exempt from registration as a CPO under the CEA.
- The person's Commodity Interest trading advice is directed solely to, and for the sole use of, the commodity pool(s) for which such person is exempt from registration as a CPO.

The above CTA registration exemption provided under CFTC Rule 4.14(a)(5) is self-executing, meaning that persons relying upon such exemption need not file notice of such exemption with the NFA.

VOLCKER RULE CONSIDERATIONS

14 Are any of the Fund's potential investors a "banking entity" within the meaning of the U.S. Bank Holding Company Act of 1956 ("Bank Holding Company Act"), a Non-U.S. banking entity with a presence in the U.S., or one of their affiliates? If yes, the Volcker Rule may apply.

Explanation: A "banking entity" may be prevented from sponsoring or making investments in investment funds pursuant to section 13 of the Bank Holding Company Act (commonly known as the "Volcker Rule"), subject to certain exemptions. Two important exemptions apply to non-U.S. banking entities. First, a non-U.S. banking entity may invest in certain "covered" funds if, among other things: (a) the banking entity satisfies certain criteria to ensure that its business is principally located outside of the United States, (b) the banking entity ensure that the decision making, the accounting treatment and the financing of the investment is outside of the United States and (c) the ownership interests of the fund are not sold in an offering that targets U.S. residents. A further exception is available to a non-U.S. banking entity that invests in foreign "non-covered funds", i.e. funds that are domiciled outside of the U.S. and that have not made any offering of securities into the U.S. Accordingly, banking entities (even ones headquartered outside the non-U.S.) may be prevented from investing in the fund if the fund has made a U.S. offering. In September 2019 further amendments were issued to exempt credit funds and venture capital funds.

KEY CONTACTS

Conrad Axelrod
Partner
+1 212 556 2314
caxelrod@kslaw.co
m

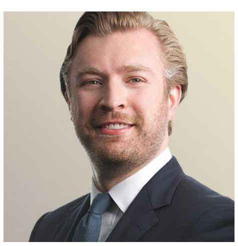
Kathryn Furman
Partner
+1 404 572 3599
kfurman@kslaw.com

Dora Chan
Senior Associate
+65 6303 6071
dchan@kslaw.com

James Stull
Partner
+971 4 377 9929
jstull@kslaw.com

Mark Davies
Partner
+813 4510 5604
mdavies@kslaw.com

John Wilson
Partner
+1 212 556 2277
jdwilson@kslaw.com



Doug Elsbeck
Partner
+1 212 556 2118
delsbeck@kslaw.com