TYPOLOGY OF PUBLIC-PRIVATE EQUITY

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ABSTRACT

Private equity, which pools funds for investment in private businesses, is one of the largest and fastest growing investment opportunities in the markets today. Private equity traditionally sought investments exclusively from sophisticated investors such as high net worth individuals and institutional investors. More recently, however, a growing number of private equity businesses have gone public and opened their doors to public investors, who are drawn to these investments because of the possibility of high returns and the opportunity to diversify their investment portfolios. In this Article, I review the universe of public-private equity (or PPE) businesses that are traded on the United States stock exchanges to map out how PPE has engaged with public investors. I find that PPE takes a variety of organizational forms, across different jurisdictions, and seeks investments from public investors at multiple levels within the private equity structure. While this variety expands the menu of options available to public investors, ignoring the fact that there are distinct types within the PPE universe can also be the source of investor and regulatory confusion. In this Article, I organize the PPE universe into three types according to whether the public investor is investing in the private equity adviser, fund, or both. This typology catalogs a complex and heterogeneous universe of firms that are sometimes lumped together as one to provide a deeper understanding of the unique structural and governance features of each type of PPE. And, by taking a segmented view of the company, fund, and securities regulatory regimes which apply, this Article takes the first step towards constructing a clear framework through which to understand and regulate PPE.

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* Assistant Professor, UC Irvine, School of Law. skim@law.uci.edu. I am grateful to my colleagues Funmi Arewa, Erwin Chemerinsky, Seth Davis, Dan Deacon, Catherine Fisk, Jonathan Glater, Michele Goodwin, Rick Hasen, Sarah Lawsky, Christopher Leslie, Leah Litman, Omri Marian, David Min, Katie Porter, Song Richardson, Greg Shaffer, Ken Simons, Bob Solomon, and Chris Whytock for taking the time to read various drafts of this Article from its early to later stages and for providing helpful suggestions and feedback. I also benefitted from the opportunity to present this Article at various conferences and workshops. Special thanks are due to commentators Bill Bratton, John Coates, and Jim Cox at Duke's Culp Colloquium, organized by Guy-Uriel Charles and Dorothy Brown, as well as participants of the Southern California Business Law Workshop, organized by David Min and Elizabeth Pollman. UCI Law librarians Lisa Junghahn and Christina Tsou provided invaluable research assistance, and UCI Law students Yashina Burns (Class of 2016), Bryce Farrington (Class of 2018), Robin Gray (Class of 2017), Lawrence Liu (Class of 2016) and Kaitlin Wetz (Class of 2019) provided excellent research and editorial assistance. I also want to thank the editors of the *Florida State University Law Review* (Volume 44), in particular, Editor-in-Chief Elisa Walker and Executive Editor Christina Strasser for their superb leadership and dedication.

I. INTRODUCTION

Private equity refers to the business of pooling the funds of individual and institutional investors and investing those funds in the equity of non-public enterprises. Using this strategy of investing in non-public equities, some private equity funds have been able to deliver spectacular returns to their investors.[1]

Coming off of record performances in realized investments and cash distributions in 2013 and 2014, more than 2,000 private equity firms sought an estimated $700 billion of capital commitments from investors in 2015.[2] According to the American Investment

1. For example, the overall annual returns from private equity investment strategies for the Yale Endowment Fund was 30.6% from 1973 to 2006. RACHEL E.S. ZIEMBA & WILLIAM T. ZIEMBA, SCENARIOS FOR RISK MANAGEMENT AND GLOBAL INVESTMENT STRATEGIES 67 (2007); THE YALE ENDOWMENT 19 (2006); Steven N. Kaplan & Antoinette Schoar, *Private Equity Performance: Returns, Persistence and Capital Flows,* 60 J. FIN. 1791 (2005) (documenting a large degree of heterogeneity among fund returns but substantial persistence of high returns among the strongest performing private equity funds); *cf.* Douglas Cumming & Uwe Walz, *Private Equity Returns and Disclosure Around the World*, 41 J. INT'L BUS. STUD. 727 (2010) (reporting significant systematic biases in managers' reporting of fund performance); Ludovic Phalippou & Oliver Gottschalg, *The Performance of Private Equity Funds*, 22 REV. FIN. STUD. 1747 (2009) (arguing that the performance of private equity funds has been overstated, reporting an average net-of-fees fund performance of 3% per year below that of the S&P 500).

2. Antoine Drean, *Ten Predictions for Private Equity in 2015*, FORBES (Jan. 12, 2015, 2:09 PM), http://www.forbes.com/sites/antoinedrean/2015/01/12/ten-predictions-for-private-equity-in-2015/. For scale, the $700 billion that is estimated to have been invested into private equity in 2015 is equivalent to the total amount that the entire arts and culture sector contributed to the U.S. gross domestic product in 2014. Javier Panzar, *Arts and Culture Ac-*

Council (AIC), a private equity industry group, there were 4,188 private equity firms and 14,214 companies that were backed by private equity firms in the United States in 2015.[3] In its most recent press release, AIC reports that the investable capital (sometimes referred to as "dry powder") of global buyout funds stood at $608 billion in September 2017.[4]

The typical investors in private equity have been sophisticated investors such as pension funds, endowment funds, and high-net-worth individuals.[5] As a result, public investors did not have the opportunity to directly invest in private equity, until recently.

The recent decision of several private equity businesses to go public has provided public investors the opportunity to directly invest in private equity. This is a relatively recent phenomenon that peaked during the boom years immediately prior to the 2007-2009 financial crises and has continued into the post-crises period.[6]

Some have celebrated this development of public-private equity (PPE) as leveling the playing field by making high-yielding investment opportunities, once reserved exclusively for sophisticated investors, more widely available to the public.[7] Others have criticized PPE for enriching insiders at the expense of public investors.[8] Such sweeping praise and criticism of PPE, however, fails to recognize its heterogeneity.

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counted for Nearly $700 Billion in U.S. GDP, L.A. TIMES (Jan. 12, 2015, 1:49 PM), http://www.latimes.com/business/la-fi-arts-culture-gdp-20150112-story.html [https://perma.cc/QG2-TNGC].

3. *Private Equity Across the U.S.*, AM. INV. COUNCIL, http://www.investmentcouncil.org/app/uploads/pegcc18_aic-infographic_v5-2.pdf.

4. *2017 Q3 Private Equity Trends Report*, AM. INV. COUNCIL, http://www.investmentcouncil.org/app/uploads/2017-q3-aic-private-equity-trends-press-release-final.pdf.

5. The descriptor 'sophisticated' in this context is used to indicate whether investors have the capacity to appreciate the complexities and risks of investing in the capital markets or possess the opportunity and resources to directly or indirectly bargain for protections when entering into these investments.

6. While much has been written about the ways in which increased congressional scrutiny following the 2007-2009 financial crises has forced more light on the shadow of private equity, this Article focuses on private equity's own emergence from the shadow into the public domain via an initial public offering.

7. *See, e.g.*, Trevor M. Gomberg, *After the Storm: Unmasking Publicly-Traded Private Equity Firms to Create Value Through Shareholder Democracy*, 73 ALB. L. REV. 575, 575 (2010) ("With a stellar reputation and analyst praise, [Blackstone's] IPO may have a far-reaching impact on an industry thrust in the spotlight."). Blackstone is one of the world's leading private equity firms, with nearly 2,300 employees in twenty-five offices worldwide, and its portfolio companies employ more than 550,000 people worldwide. Who We Are, BLACKSTONE, https://www.blackstone.com/the-firm/overview [https://perma.cc/6LQ6-6FT6].

8. *See, e.g.*, Ronald J. Gilson & Charles K. Whitehead, *Deconstructing Equity: Public Ownership, Agency Costs, and Complete Capital Markets*, 108 COLUM. L. REV. 231, 260 n.140 (2008) ("The result is liquidity for Blackstone's owners at relatively low cost to them, but potentially resulting in substantial agency costs being borne by the unitholders.").

This Article reviews the universe of PPE to explain why and how private equity firms and funds have made the decision to go public. I examine the initial public offerings (IPOs) of forty-two PPE firms, which have a total market capitalization of more than $111 billion, to uncover the depth and breadth of the PPE segment. I review the company reports, regulatory filings, and organizational documents of these firms to understand the motivations and manner of how these private equity businesses have made the decision to go public.

What I find from this review is that the PPE universe is made up of different types of organizational forms (corporation, limited liability company, limited partnership, and trust) and funds (open-end, closed-end, internally-managed,[9] and externally-managed). While the well-known private equity groups such as Blackstone, Apollo, Carlyle, and Fortress have received the most attention and have been written about as representative examples of PPE, they are only a subset of this large, growing, and diverse segment of firms.[10]

My assessment of PPEs is that they are hybrid organizations that retain some but not all features of private equity and adopt some but not all features of a public company. This hybridity creates challenges for their regulation and demonstrates the need for a typology that can be used to organize the PPE universe.

The tier at which public investors invest affects their economic rights, voting rights, the disclosures they will receive, as well as the nature of fiduciary relationships.[11] Based on this observation that the level at which the public investor invests is an important determinant of the key features that organizational, fund, and securities regulatory regimes care most about, this Article offers a typology that catalogs the PPE universe on this dimension.

I sort the PPE universe across three types. The first type of PPE offers to public investors shares of the manager (i.e., the entity that raises, invests, and manages underlying private equity funds) and / or adviser (i.e., the entity that advises the underlying private equity funds) of a private equity fund. The second type of PPE offers to public investors shares of the private equity fund (i.e., the investment company providing equity to operating businesses). The third type of

9. An "internally-managed" fund is a fund that has no investment adviser and is internally managed by its executive directors under the supervision of its board of directors.

10. *See* Brian Cheffins & John Armour, *The Eclipse of Private Equity*, 33 DEL. J. CORP. L. 1, 1 (2008); Steven M. Davidoff, *Black Market Capital*, 2008 COLUM. BUS. L. REV. 172, 237-38; Lloyd L. Drury, III, *Publicly-Held Private Equity Firms and the Rejection of Law as a Governance Device*, 16 U. PA. J. BUS. L. 57, 62-66 (2013); Gilson & Whitehead, *supra* note 8, at 251-56.

11. *See infra* Part III for a discussion of the structural, governance, and regulatory characteristics of each PPE type.

PPE offers to public investors shares of both the manager / adviser and fund entities within the private equity group.

The main contributions made by this Article are two-fold. First, this Article uncovers the complexity and heterogeneity of the PPE universe to explain and classify a new generation of private equity. This Article also offers the most expansive account of PPE to date by reviewing the universe of forty-two firms with a total market cap of $111 billion.

Second, by taking a segmented view of the company, fund, and securities regulatory regime that apply to PPE, this Article provides a clear framework through which to organize and regulate PPE. I identify the features of each PPE type that are most perilous to public investors and make a first attempt to match each type to the regulatory regime that is most effective at addressing such perils. This segmented and tailored view of regulations is not only useful for PPE but could also be extended to other hybrid organizations that are subject to multiple regulatory regimes, which may sometimes be in tension with one another.[12]

Part II provides an overview of private equity, PPE, and the heterogeneity within the PPE universe to demonstrate the need for a typology. Part III organizes the PPE universe according to the public investor's position within the private equity structure. Part IV puts the typology to work by matching each PPE type with the multiple regulatory regimes, namely applicable organizational laws, fund regulations, and securities regulations. Part V concludes.

II. PRIVATE EQUITY AND PUBLIC-PRIVATE EQUITY (PPE)

Private equity, as its name suggests, has many private qualities. Quintessential private equity raises money through private placements.[13] Once a private equity sponsor has identified a target, the standard course of action is for the sponsor to take the target company, if a public company, private.[14] The identity of owners and investors, investment strategies, and profits and losses of private equity firms and funds are not typically known to outsiders,[15] including regulators.[16]

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12. Frank Partnoy, *Shapeshifting Corporations*, 76 U. CHI. L. REV. 261, 265-67 (2009).

13. *See* Josh Lerner, *Venture Capital and Private Equity: A Course Overview* 12 (Harv. Bus. Sch. Working Paper, No. 98-042, 1997).

14. *Id.* at 12-18 (describing the standard features of private equity firms and noting that "[p]rivate equity investors are almost invariably attracted to firms that find traditional financing difficult to arrange").

15. Steven E. Hurdle, Jr., Comment, *A Blow to Public Investing: Reforming the System of Private Equity Fund Disclosures*, 53 UCLA L. REV. 239, 243-44 (2005) ("Most private equity funds and investors appear to agree that keeping investment details confidential benefits all parties because '[limited partners] want to earn the best return possible

Private equity, in the shadows of regulation, has generated impressive returns for its investors. The private equity model has also been praised for reducing agency costs that are endemic to publicly-held companies.[17] Michael Jensen went so far as to predict in his classic 1989 article that the private equity model of corporate ownership would contribute to the 'eclipse' the public corporation.[18] More recently, Michael Ewens and Joan Farre-Mensa attributed the decline in initial public offerings in the United States to the growing supply of capital from private funds, such as private equity.[19]

With most of the academic discourse focused on the ways in which private equity has displaced public markets, the decision by private equity firms and funds to go public is quite a contradiction that defies expectations.[20] While this development can be good for investors, as it expands the menu of investments, and good for the markets, as a channel for diffusion of the innovations originated by private equity,[21] it is important to recognize that it is the *sponsors* of private equity—not investors or market regulators—that control the decision of whether, when, and how to make the switch from the private to the public realm. And any sweeping statement as to the impact of this development on investors and markets fails to recognize the diversity within this universe.

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and [general partners] want to safeguard sensitive information about the private companies in which they invest.' " (quoting Mark Heesen, *Public Transparency Must Be Balanced with Protecting Private Data*, 2003 VENTURE CAP. J. 44).

16. Private equity firms fit under the private placement exemption, which relieves them from the disclosure obligations related to a public offering. James C. Spindler, *How Private Is Private Equity, and at What Cost?*, 76 U. CHI. L. REV. 311, 321 (2009).

17. Notably, Professor Michael Jensen has praised the private equity model for its ability to reduce agency costs by using high leverage and pay-for-performance compensation. *See* Michael C. Jensen, *Eclipse of the Public Corporation*, HARV. BUS. REV., Sept.-Oct. 1989, at 61, http://hbr.org/1989/09/eclipse-of-the-public-corporation/ar/1 [https://perma.cc/REH7-PWCZ].

18. *Id.*

19. Michael Ewens & Joan Farre-Mensa, *The Evolution of the Private Equity Market and the Decline in IPOs* (Cal. Inst. Tech., Working Paper 2018), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3017610 [https://perma.cc/8NVQ-CU3A] (reporting that more firms are able to raise capital while staying private because of the growth in the supply of private capital from venture capital and private equity funds).

20. Steven Davidoff Solomon characterizes the private equity structure as one that is "path dependen[t]" and "stick[y]." Steven M. Davidoff, *The Failure of Private Equity*, 82 S. CAL. L. REV. 481, 527 (2009).

21. Elisabeth De Fontenay, *Private Equity Firms as Gatekeepers*, 33 REV. BANKING & FIN. L. 115, 132 n.84, 169 (2013-2014) (noting the "frequent innovations in debt terms that originate with private equity-related financings" and "[o]ne of the skills developed by private equity firms is the ability to recognize and act on 'mispricings' between the debt and equity markets").

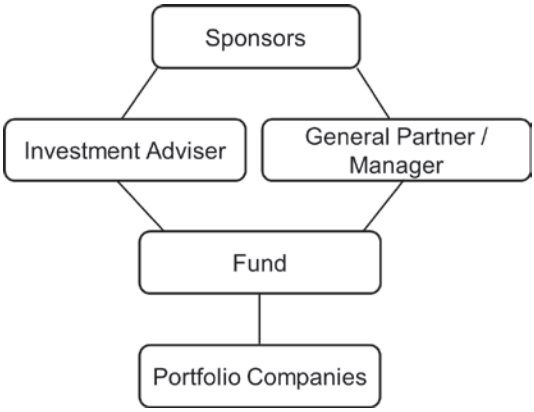
A. *Private Equity Primer*

Private equity refers to the business of pooling the funds of individual and institutional investors and investing those funds in private enterprises. This simple definition of private equity demonstrates one of its appeals—private equity offers investors an opportunity to invest in private businesses that are not otherwise readily available to buy and sell in the public markets.[22]

Private equity has been one of the largest and fastest-growing asset classes in finance. Hitting record performance levels in realized investments and cash distributions in 2013 and 2014, more than 2,000 private equity firms sought an estimated $700 billion of capital commitments from investors in 2015.[23] According to the American Investment Council, there were 4,188 private equity firms and 14,214 companies backed by private equity firms in the United States in 2015.[24]

Below is a diagram of the prototypical private equity structure, which also forms the basis for the typology presented in Part III.

Figure 1. Prototypical Private Equity Structure



The **sponsors** are the individuals or entities that solicit investments from investors into the private equity fund. The private equity investment model can be broken down into three functions, each of which is typically overseen by separate entities created by the spon-

22. *See, e.g.*, Stephen Foley, *Private Equity Begins to Entice Ordinary Investors*, FIN. TIMES (May 26, 2015), http://www.ft.com/intl/cms/s/2/e85240c4-b150-11e4-831b-00144feab7de.html#axzz44xp6hRzp [https://perma.cc/YWW7-M4P3] ("Investors able to take a long-term view, who are seeking returns potentially higher and uncorrelated to the equity markets, could find private equity an intriguing, if risky, alternative.").

23. Drean, *supra* note 2.

24. *Private Equity Across the U.S.*, *supra* note 3.

sors: (1) the **investment adviser** provides investment advisory services to the fund; (2) the **general partner** or **manager** has the legal power to control, administer, and take actions on behalf of the fund; and (3) the **fund** pools and holds capital from outside investors.

Private equity funds typically acquire a controlling or influential ownership interest in the businesses in which they invest, also referred to as their **portfolio companies**.[25] The private equity investment structure generates returns through income (e.g., interest, dividends, or fees) and capital gains that are realized by the sponsors' eventual exit from their investments in their portfolio companies, usually within a three- to five-year term.[26]

The private equity structure is arranged this way to take advantage of economies of scale, tax benefits, limited liability, and regulatory arbitrage opportunities, among other reasons. The investment adviser often acts in an advisory capacity for multiple funds raised by the same sponsor, which leads to cost savings from economies of scale.[27] The general partner or manager, as the managing entity with legal power to act on behalf of the fund, will generally be liable for claims against the fund, and the sponsors insulate themselves from this general liability by creating a separate entity to perform these managerial functions.[28] The fund is typically formed as a limited partnership (the investors being the limited partners of the fund) so that the entity will be considered a 'pass-through' entity for federal income tax purposes.[29]

John Morley has studied the pattern of separation of investment and management in funds and how this separation limits investors' control of managers. He explains that the separation between investors and managers actually benefits investors by limiting their con-

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25. This controlling stake provides private equity sponsors with the ability to implement necessary improvements and changes within their portfolio companies. Private equity funds often require the executives of the portfolio company to take an ownership share so that these executives also have skin in the game. *See* JAMES M. SCHELL ET AL., PRIVATE EQUITY FUNDS: BUSINESS STRUCTURE AND OPERATIONS § 1.01 (2015).

26. A number of levers are used by private equity sponsors to discipline the executives of portfolio companies, such as executive compensation and corporate governance arrangements, which require that employees or designees of private equity sponsors sit on the board of the portfolio company. *See, e.g.*, Ronald W. Masulis & Randall S. Thomas, *Does Private Equity Create Wealth? The Effects of Private Equity and Derivatives on Corporate Governance*, 76 U. CHI. L. REV. 219 (2009) (describing the corporate governance advantages of private equity).

27. John Morley, *The Separation of Funds and Managers: A Theory of Investment Fund Structure and Regulation*, 123 YALE L.J. 1228, 1233 (2014).

28. SCHELL, *supra* note 25.

29. Patrick Fenn & David Goldstein, *Tax Considerations in Structuring U.S.-Based Private Equity Funds*, INT'L FIN. L. REV. 1 (2002), http://www.iflr.com/Article/2027251/Tax-considerations-in-structuring-US-based-private-equity-funds.html [https://perma.cc/8WAP-HUXV].

trol and exposure to liabilities.[30] These investors instead rely on extralegal mechanisms to ensure that their investments are protected.[31] But what happens (and what should happen) when private equity expands its investor base to public investors who may have different preferences and capacities to monitor managers as compared to the usual investors in private equity funds? To answer this question, I first present a descriptive survey of public-private equity firms and funds to expose the diversity within this segment and to demonstrate the need for a typology to better understand it.

B. Public-Private Equity

While private equity firms and funds have traditionally been organized as unregistered private entities, more and more are choosing to go public. What motivates the decision to go public? As a general matter, private firms suffer from liquidity constraints because they are limited as to the number and type of investors they can accept investments from. On the other hand, public firms suffer from the collective action and agency problems that arise from dispersed ownership and the separation of such owners from those who control the firm.[32]

The reasons why private equity sponsors, in particular, may decide to launch an IPO are numerous. One reason is prompt and flexible access to funds.[33] An IPO allows a private equity fund to seek alternative sources of capital and build a rotating but permanent capital base for funds.[34] This permanence is especially useful amidst economic downturns, such as the recent 2007-2009 financial crisis, during which it was difficult for private equity funds to rely on private investors as the exclusive source of funds.[35]

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30. Morley, *supra* note 27, at 1240-41.

31. Usha Rodrigues & Mike Stegemoller, *Exit, Voice, and Reputation: The Evolution of SPACs*, 37 DEL. J. CORP. L. 849, 854 (2013) ("[R]eputational constraints hold the richly dynamic tension between traditional private equity investors and managers largely in equilibrium.").

32. Kristian D. Allee et al., *Private Versus Public Corporate Ownership: Implications for Future Profitability* 3 (Kelley School of Business, Working Paper No. 2014-16, 2015), http://ssrn.com/abstract=2375916 [https://perma.cc/HT76-BQUU] (discussing the effect of public versus private ownership on firm profitability).

33. Mohsen Manesh, *Legal Asymmetry and the End of Corporate Law*, 34 DEL. J. CORP. L. 465, 499 (2009) ("Rather than ensuring distributions to the owners and thereby forcing the managers to return to the capital markets in pursuit of cash, [private noncorporations] . . . go public partly in order to get 'permanent' capital.").

34. Orit Gadiesh, *When Private Equity Goes Public*, FORBES (Jun. 15, 2007, 6:00 AM), https://www.forbes.com/2007/06/14/bain-private-equity-oped-cx_og_0615bain.html#1f7dd3f81bff ("The upside is that the firms don't need to waste time and precious human capital on fund-raising, a time-consuming process that takes some of the vital players in a private equity firm off the field every few years for months at a time.").

35. Thomas Heath, *Private Equity Had Role in Crisis, Says Carlyle Co-Founder*, WASH. POST (Oct. 14, 2009), http://www.washingtonpost.com/wp-dyn/content/

Another reason some private equity sponsors may choose to go public is the value of public equity as currency. The ease of monetization and valuation of the company's shares allows private equity sponsors to attract and retain qualified employees using incentives or stock options that are pegged to the value of the company's publicly-traded shares.[36]

Other important motivators include the legacy effect, reputational effect, and the status and visibility that comes with being a public company.[37] Private equity funds are often associated with its founder, and the decision to go public can form the core of a succession plan and vision for the company that lasts beyond the founder's term. Also, the rigorous Securities Exchange Commission (SEC) disclosure requirements and public scrutiny can be expected to improve transparency and accountability of these firms and funds.[38]

The calculus for private equity sponsors is then whether such valuation, liquidity, and reputational benefits of going public are worth the increased regulatory scrutiny, liability, and related costs that come from being a public company. PPE takes a variety of forms that reflect the different calculus that has been reached among the differing PPE sponsors.

In the remainder of this Section, I share some findings from my review of forty-two PPEs. All of the details regarding the firms are drawn from publicly available sources. The primary sources cited are the registration statements, charters, prospectuses, and periodic reports of each firm. All of these sources are publicly available on the SEC's website. Additional details are drawn from the company's investor relations page as well as media and analysts' reports.

I constructed the universe of public-private equity firms by first running the below company search criteria on Bloomberg.

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article/2009/10/13/AR2009101303014.html [https://perma.cc/E63N-5GHE] (reporting on Carlyle Group co-founder David M. Rubenstein's comments made in 2009 that private equity is in "a lull" because of difficulty in accessing credit).

36. Gadiesh, *supra* note 34 ("Finally, the leading funds have clearly developed their own brands. Taking a page from their own playbooks for growing the value of their portfolio companies, they see ways to use their brands to raise more capital, extend their range and pursue more opportunities.").

37. *Id.* ("Another benefit is differentiation. Money, after all, is rapidly becoming a commodity, and leading private equity funds are looking for ways to stand out even further from the crowd.").

38. Donald C. Langevoort & Robert B. Thompson, "*Publicness" in Contemporary Securities Regulation After the JOBS Act*, 101 GEO. L.J. 337, 340 (2013); Hillary A. Sale, *Public Governance*, 81 GEO. WASH. L. REV. 101 (2013).

Table 1: Search Strategy

Type:	Search (Company)
Country:	Matches any of the following: **United States**
Industry:	Matches any of the following: **Private Equity**[39]
Trading Status:	Matches any of the following: **Active**

I reviewed the list and excluded firms that were as of September 1, 2016 either: (1) no longer active or (2) upon reviewing the company business description in the most recent Form 10-K, no longer operating within the private equity segment. The private equity segment is defined as firms and funds that are in the business of providing equity financing to private companies. I supplemented this list with the firms that are included in five indexes[40] of public-private equity firms

39. "Private Equity" is defined by Bloomberg as investments in "equity capital not offered on the public exchange. For example, investments made directly into a private company; e.g., buyouts." Technical conversation with Research Specialist, BLOOMBERG BNA (June 6, 2016).

40. These indexes are:

1. S&P Listed Private Equity Index: The S&P Listed Private Equity Index comprises the leading listed private equity companies that meet specific size, liquidity, exposure, and activity requirements. *S&P Listed Private Equity Index*, S&P DOW JONES INDICES, http://us.spindices.com/indices/equity/sp-listed-private-equity-index [https://perma.cc/62A2-2FP4].

2. PowerShares—PSP Global Listed Private Equity Index: The PSP Index includes securities, American depository receipts, and global depository receipts of 40 to 75 private equity companies, including business development companies (BDCs), master limited partnerships (MLPs), and other vehicles whose principal business is to invest in, lend capital to, or provide services to privately held companies (collectively, listed private equity companies). *PSP—PowerShares Global Listed Private Equity*, INVESCO, https://www.invesco.com/portal/site/us/financial-professional/etfs/holdings/?ticker=PSP [https://perma.cc/6MED-5PKD].

3. ALPS | Red Rocks Listed Private Equity Fund: The ALPS | Red Rocks Listed Private Equity Fund is an open-end mutual fund that invests in publicly-traded private equity companies that trade on global exchanges. The Fund assembles approximately 30 to 50 holdings and is diversified by stage of investment, geography, industry, and capital structure. *ALPS: Red Rocks Listed Private Equity Fund*, ALPS, http://www.alpsfunds.com/holdings/alps-red-rocks-listed-private-equity-fund [https://perma.cc/2U29-WEFS].

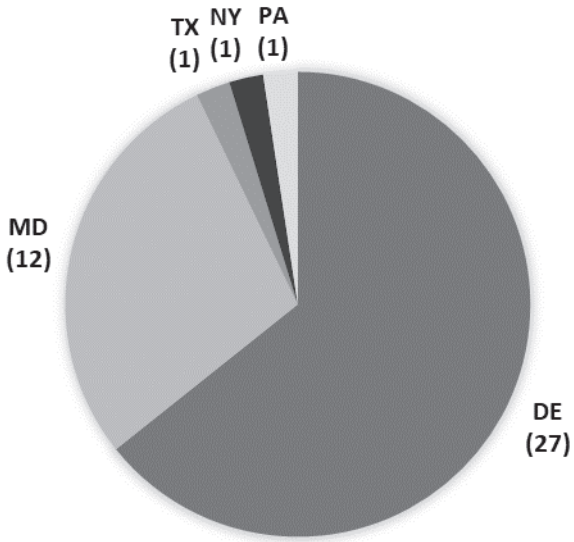
4. iShares Listed Private Equity UCITS ETF: The iShares index tracks the performance of an index composed of publicly-listed companies active in the private equity space. *iShares Listed Private Equity UCITS ETF*, ISHARES, https://www.ishares.com/uk/individual/en/products/251918/ishares-listed-private-equity-ucits-etf?siteEntryPassthrough=true [https://perma.cc/8Z3X-VU6Q].

5. LPX Direct Listed Private Equity Index: The LPX Direct represents the most actively traded LPE companies covered by LPX Group that mainly pursue a direct private equity investment strategy. A listed private equity company is

(limiting the sample to domestically-organized and domestically-traded firms), bringing the total number of firms to forty-two.[41]

Twenty-seven of the forty-two PPEs are organized in Delaware, and twelve of the forty-two PPEs are organized in Maryland. One firm is organized in New York, one in Pennsylvania, and one in Texas.

Chart 1: PPE Jurisdiction

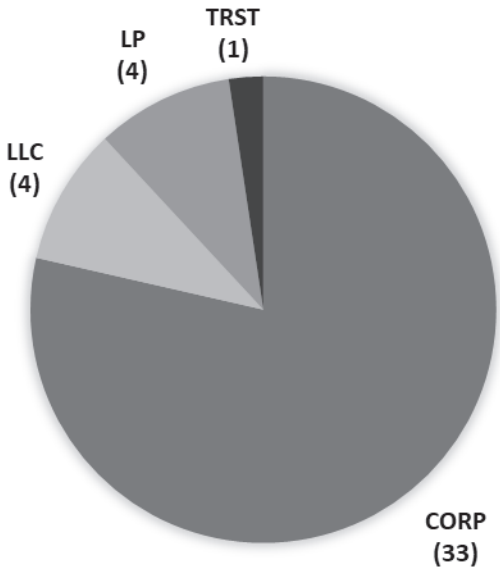


Thirty-three of the forty-two PPEs are organized as a corporation. Four are limited partnerships and four are limited liability companies. One firm is organized as a trust.

an eligible candidate for the Index if its direct private equity investments, as well as cash and cash equivalent positions and post-Initial Public Offering listed investments, represent more than 80% of the total assets of the company. *LPX Direct*, LPX, http://www.lpx-group.com/lpx/lpx-index-family/style-indices/lpx-direct.html [https://perma.cc/AWK3-JSKG].

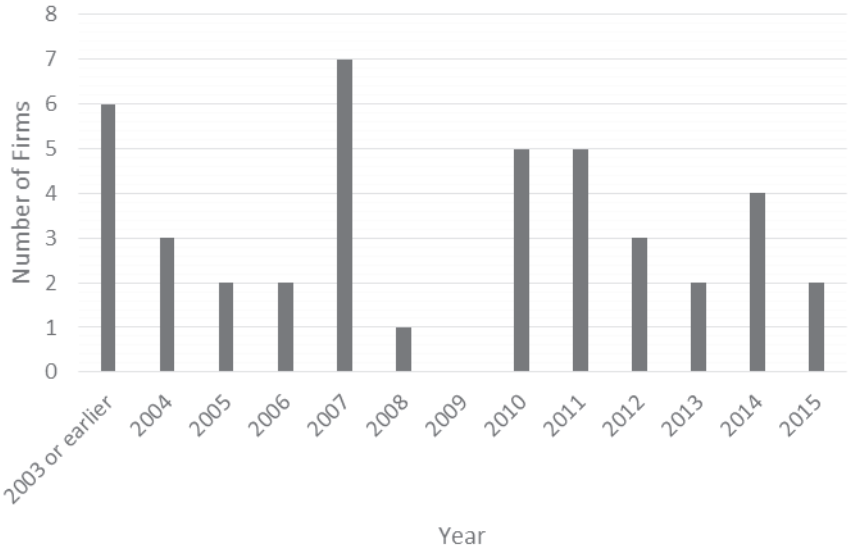
41. See Appendix for a list of the forty-two firms, their ticker symbols, the stock exchanges on which their shares are traded, and their total market capitalization (as of Sept. 1, 2017).

Chart 2: PPE Organizational Form



There were six PPEs that were already public before the year 2004. Since then, there has been a steady stream of PPEs that have made the decision to go public every year (except in 2009).

Chart 3: PPE IPO Timing



The issuer of publicly-traded shares is sometimes the management company (i.e., the entity that raises, invests, and manages un-

derlying private equity funds) or adviser (i.e., the entity that advises the underlying private equity funds). In these cases, the issuer of publicly-traded shares is often a holding company that has been specifically created for the purposes of the public offering. Among the forty-two PPEs that I reviewed, fourteen issued shares at the management company and / or adviser level. In other cases (twenty-eight of the forty-two PPEs), the issuer of publicly-traded shares is the investment company (i.e., the fund providing equity to operating businesses). There were six cases (or three pairs of cases) where both the manager and fund entities within the same private equity structure issued shares to the public.

C. Demonstrating a Need for an Investor-Focused Typology

As demonstrated by the earlier discussion, PPEs represent a diverse and varied segment: PPEs are organized as corporations, limited liability companies, limited partnerships, and business trusts in Delaware, Maryland, New York, Texas, and Pennsylvania. More importantly, PPEs issue shares to the public at every level of the private equity structure—the management company, holding company, and investment company. And, while this diversity is good for public investors in that it expands the menu of investments, it also presents challenges to understanding each option on the menu.

At the one end of two extremes, the holder of a unit of the investment company will receive a share of capital gains and income, while at the other end, the holder of a unit of the manager or adviser entity will receive a share of the manager or adviser's compensation. Steven Davidoff Solomon has explained how investing in a public-private equity manager or adviser is much riskier than investing directly in the funds.[42] This is because the future income of an adviser is dependent on the adviser's continued ability to earn extraordinary positive returns. However, investing in the fund directly has its own risks, as I later explain.

There are two key observations to be made here. First, there are very good reasons from the *sponsors'* perspective to explain the particular way any given PPE is structured. The sponsors' goal is to maximize returns and minimize the liability exposure to the sponsors in the event of loss. Certainly, the sponsors' desire to maximize their returns while minimizing liability has led to new innovations in the marketplace, as discussed above. But the second takeaway is that applicable regulations are intended to benefit parties other than the sponsor and designed to achieve broader objectives beyond facilitating innovation. This Article evaluates PPE from the perspective of

42. Davidoff, *supra* note 10, at 237-38.

the intended beneficiaries and desired objectives of the regulations to which PPE are now subject.

What are these laws and regulations? In the remainder of this Section, I preview the regulations that apply to PPE before turning to the typology that organizes the PPE universe according to the dimensions that these regulations are designed to address.

First, organizational laws (corporate, limited liability company, partnership, and trust laws) provide businesses with various organizational forms that possess the attributes desired by most such businesses. Taking corporate law as an example, one primary function of corporate law is to provide businesses with a legal form that possesses the core attributes of a business that wishes to incorporate.[43] Henry Hansmann and Reinier Kraakman have identified these core attributes as: legal personality, limited liability, transferable shares, delegated management, and investor ownership.[44]

Another function of corporate law is to mitigate the agency costs that arise from the separation of ownership and control.[45] The separation of ownership and control refers to a few managers exercising control of a company on behalf of its many owners.[46] This separation overcomes collective action problems but generates agency costs. Agency costs refer to the costs of monitoring the agent (managers) to ensure that the agent acts in the best interests of the principal (shareholders of the company).[47] The conflicts of interest that give rise to these agency costs occur between managers and shareholders, among shareholders, and between shareholders and other constituents, such as employees or creditors.[48]

Robert Bartlett's study of venture capital finance was the first to bring attention to the horizontal (inter-investor) agency problems in funds.[49] Specific to the private equity context, William Birdthistle and Todd Henderson have identified the inter-fund conflicts that re-

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43. Henry Hansmann & Reinier Kraakman, *What is Corporate Law?*, *in* THE ANATOMY OF CORPORATE LAW: A COMPARATIVE AND FUNCTIONAL APPROACH 1, 2 (2004) ("Self-evidently, a principal function of corporate law is to provide business enterprises with a legal form that possesses these five core attributes [of the business corporation].").

44. *Id.* at 1 (listing the five basic legal characteristics of the business corporation).

45. *Id.* at 2 ("[A] second, equally important function of corporate law . . . is, constraining value-reducing forms of opportunism among the constituencies of the corporate enterprise.").

46. ADOLF A. BERLE, JR. & GARDINER C. MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY 119-25 (1948).

47. FRANK H. EASTERBROOK & DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW 10 (1991).

48. Hansmann & Kraakman, *supra* note 43, at 2 (listing the three principal conflicts with the corporation).

49. Robert P. Bartlett, III, *Venture Capital, Agency Costs, and the False Dichotomy of the Corporation*, 54 UCLA L. REV. 37 (2006).

sult from the diversification strategies of private equity investors.[50] These insights can be carried over to PPE to show that the relative position of the public investor vis-à-vis other investors has important implications for prospective conflicts of interest, which corporate law aims to mitigate.

Second, fund and fund adviser regulations are intended to address the conflicts of interest that arise from both the nature of assets held by funds and the separation of funds and managers. The primary regulatory regimes are the Investment Company Act of 1940[51] and the Investment Advisers Act of 1940.[52] John Morley explains that the most important characteristic of funds (which hold investment assets) is that they are separated from managers (who hold management assets) into different entities with different owners.[53]

While this separation of funds and managers may be beneficial to the investors of funds,[54] I show that because public investors in PPE invest at not only the fund but also the manager and adviser levels, the analysis of what is good for the investors of funds is necessarily incomplete when it comes to evaluating the best interests of public investors in PPE.

Third, we regulate companies that issue securities to the public differently from those that draw funds from private investors.[55] PPE, by going public, is swept into the public company regulatory regimes. The primary regulations are the Securities Act of 1933 (the 1933 Act)[56] and the Securities Exchange Act of 1934 (the 1934 Act).[57] The stated goals of such regulatory regimes are investor protection, capital formation, and the stability of the overall financial system.[58]

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50. William A. Birdthistle & M. Todd Henderson, *One Hat Too Many? Investment Desegregation in Private Equity*, 76 U. CHI. L. REV. 45, 54-55 (2009).

51. The Investment Company Act of 1940 was originally enacted as Chapter 686, Title I, sections 2-906, and is now codified as 15 U.S.C. §§ 80a-1 et seq.

52. The Investment Advisers Act of 1940 was originally enacted as Chapter 686, Title II, sections 201-244, and is now codified as 15 U.S.C. §§ 80b-1 et seq.

53. Morley, *supra* note 27, at 1258, 1279.

54. John Morley argues that the use of separate entities to hold management assets and investment assets limits fund investors' rights and risks in three distinct ways that are desirable to the investment enterprise: First, it limits the exposure of fund assets to the liabilities and creditors of the management company. Second, it limits the exposure of fund investors to the liabilities and creditors of the management company. And third, it limits fund investors from exercising residual control over the management company. *Id.* at 1240-41.

55. Private issuers sometimes are also subject to reporting requirements. Robert P. Bartlett, III, *Going Private but Staying Public: Reexamining the Effect of Sarbanes-Oxley on Firms' Going-Private Decisions*, 76 U. CHI. L. REV. 7, 16-20 (2009).

56. 15 U.S.C. § 77a.

57. 15 U.S.C. § 78a.

58. Langevoort & Thompson, *supra* note 38, at 337-38 ("Part of the stress [on securities regulation] is political, as we debate the right balance among investor protection, the

However, since not every level of the private equity structure goes public, only the entity that offers its shares to the public is subject to public company regulations, although some disclosures are made on a consolidated basis. This inconsistency can be confusing and misleading to the investor. The next Part offers a typology to help understand and organize the PPE universe by the investor's point of entry, which, as I explain below, is the dimension with which organizational, fund, and securities regulatory regimes are most concerned.

III. PPE TYPOLOGY

To summarize the earlier discussion regarding the various regulatory regimes that apply to PPE: organizational laws aim to facilitate the core attributes desired by businesses and to mitigate agency costs; fund and adviser regulations aim to mitigate the conflicts of interest that arise between fund advisers and fund investors; and securities regulations aim to protect investors and facilitate capital formation.

For each PPE type, I discuss the issuer, offering, and investor characteristics that organizational, fund, and securities laws and regulations care about the most. These include their **structure**: Which entity is the issuer and what is the public investor getting a share of? Who are the investors in this layer of the private equity structure and in other layers? What is the relationship of the issuer to other entities within the private equity structure? They also include their **governance** features: Who makes key decisions? Who is in control, and are there any limits on public investors' right to vote on key decisions? Where do potential conflicts of interest arise? I also discuss applicable **regulations** and exemptions, as well as the trends I observe in my review of the firms within that type and include illustrations using examples from my review of PPEs.

A. PPE Type 1: Public-Private Equity Manager

Under this structure, the manager and / or adviser of the private equity fund is the entity whose shares are being offered to public investors. In this PPE type, the public investors are situated above the funds that are managed by the manager and below the sponsors that continue to make key decisions for the entire PPE structure.

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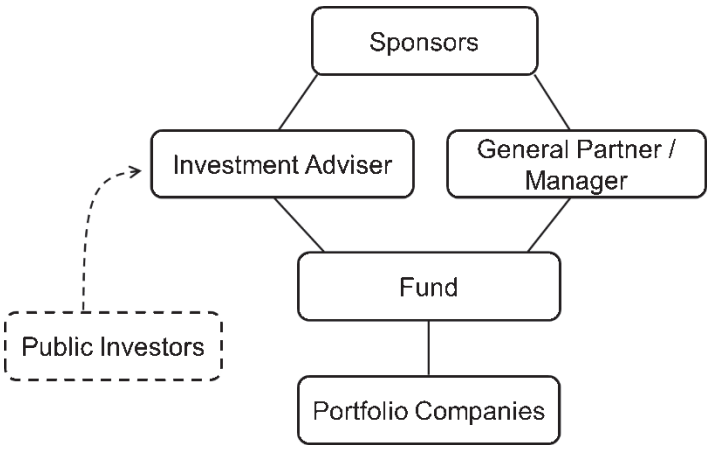
public's interest in a safe and stable financial system, and the needs of private enterprise for access to capital . . . .").

Figure 2: PPE Type 1 (PPE Manager)



1. Structure

PPE Type 1 (or **PPE Manager**) serves a managerial or advisory role for the underlying funds. The private equity funds that PPE Type 1 manages continue to draw investments from private investors (unless the fund entity has also offered its shares to public investors, which is separately discussed as PPE Type 3 below). These private investors have committed to contributing a specific amount of capital to the funds in the traditional ways that private equity draws funds from investors.[59]

PPE Type 1 earns management fees in accordance with contractual arrangements that it has entered into with the funds that it manages. PPE Type 1 receives an incentive fee (also referred to as carried interest[60]), which is paid if investment return targets are met by the funds that it manages. If PPE Type 1 also acts as the investment adviser, it will earn advisory fees for the transaction advisory and oversight services it provides to the portfolio companies of the funds that it manages. A public investor holding a share

59. The general partner will often invest its own capital in the fund (generally ranging from 2-5% of a fund's total capital commitments). PRIVATE EQUITY INT'L, FUND FORMATION AND INCENTIVES REPORT (2014), https://www.srz.com/images/content/5/7/v2/57490/SRZ-PEI-Fund-Formation-and-Incentives-Report.pdf [https://perma.cc/ABZ9-JRTV] (reporting that 79% of general partners surveyed contributed more than 1% of the total fund size with their own funds).

60. The tax treatment of the carried interest as capital gains rather than ordinary income has been a highly contested issue. *Compare* Victor Fleischer, *Two and Twenty: Taxing Partnership Profits in Private Equity Funds*, 83 N.Y.U. L. Rev. 1 (2008) (arguing that the carried interest "loophole" should be closed) *with* Steve Judge, *Why Carried Interest Is a Capital Gain,* N.Y. TIMES (Mar. 4, 2013), https://dealbook.nytimes.com/2013/03/04/why-carried-interest-is-a-capital-gain/ [https://perma.cc/9ZQG-Y3WQ].

of PPE Type 1 will receive its pro rata share of the above described fees earned by the manager and / or adviser.

In some cases, the sponsors will form a new entity specifically for the public offering. The new entity (or holding company) holds and controls the private equity adviser and / or manager entities. One of the benefits of a holding company structure is that it gives sponsors a blank slate, which provides them with the flexibility to choose from a wide range of economic and governance arrangements, as outlined below.

2. Governance

There are three principal strategies used (often in combination) by sponsors to retain control over PPE Type 1, even following its public offering. The first strategy is to cap the percentage of shares of PPE Type 1 offers to the public. The second is to use a dual class structure where one class of shares is offered to the public and another class of shares is offered to the sponsors and other insiders for the purpose of granting voting power to those insiders. Third, the sponsors may enter into contractual arrangements with public investors that provide the sponsor with exclusive or outsized voting power.

Another feature that is frequently observed in PPE Type 1 is the limited call right. This right is triggered when unitholders (other than the sponsors and other insiders) hold less than a specified percentage of the then issued and outstanding units. Once triggered, the issuer has the right, which it may assign in whole or in part to any affiliate, to acquire all of the remaining units of the class or series held by unitholders (other than the sponsors and other insiders), subject only to advance notice requirements.[61]

3. Regulation

PPE Type 1 avails itself of a number of exemptions under the Investment Company Act.[62] One strategy commonly used by sponsors is to rely on the exemption set forth in Section 3(a)(1) of the Investment Company Act by structuring PPE Type 1 such that the assets and income derived from the investment securities of the entity fall under the 40% threshold.[63] Alternatively, sponsors have also relied on the

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61. *See, e.g.*, Oaktree Capital Group, LLC, Registration Statement (Form S-1) 189 (June 17, 2011) [hereinafter Oaktree Capital (Form S-1)], https://www.sec.gov/Archives/edgar/data/1403528/000119312511167852/ds1.htm [https://perma.cc/8KF5-ZLK3].

62. Investment Company Act of 1940, 15 U.S.C. §§ 80a-1 to 80a-64.

63. 15 U.S.C. § 80a-3(a)(1)(c). To show that PPE holds investment securities with a value that does not exceed 40% of their total assets, PPE Type 1s for purposes of defining "investment securities" count limited partnership interests in the funds they manage, but not general partnership interests if profits are derived from efforts of the general partners.

exemption set forth in section 3(b)(1) of the Investment Company Act[64] by arguing that PPE Type 1 is a separate entity from the fund, and therefore, it is not engaged in the investment company business. The SEC has, from time to time, been persuaded by this argument and has made the determination that certain PPE Type 1s are not an investment company; rather, they are in the business of providing asset management and financial advisory services to others.[65]

While PPE Type 1 may avoid regulation as an investment company, as investment advisers to the investment funds they manage, they fall squarely under the regulatory scope of the Investment Advisers Act.[66] Notably, the Investment Advisers Act places restrictions on management fees payable to PPE Type 1s by the investment funds they manage and advise.[67] These rules are not compatible with private equity fund incentive structures that compensate managers using a combination of management fees based on the amount invested, transaction and advisory fees, and carried interest.[68]

PPE Type 1 has avoided these restrictions by availing itself of exemptions, including amounts that are received from: (1) any private equity fund that meets the criteria specified in section 3(c)(7) of the Investment Company Act, (2) a "qualified client," (which is determined by the assets and net worth of the client), (3) a U.S. nonresident, or (4) a "business development company" ("BDC") (which is determined by the nature of the portfolio companies in which in the fund invests).[69] The Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) narrowed certain of these exemptions, for example by directing the SEC to adjust the dollar amounts used to determine whether a client is a "qualified client."[70] In addition, the Dodd-Frank Act also eliminated the private investment adviser exemption that had permitted advisers with fewer than fifteen

64. 15 U.S.C § 80a-3(b)(1).

65. *Initial Public Offerings of Investment Managers of Hedge and Private Equity Funds: Hearing Before the S. Comm. on Fin.*, 110th Cong. (2007) (statement of Andrew J. Donohue, Director, Division of Investment Management, SEC).

66. Investment Advisers Act of 1940, 15 U.S.C. §§ 80b-1 to 80b-21.

67. 15 U.S.C. § 80b-5(a) ("No investment adviser registered or required to be registered with the Commission shall enter into, extend, or renew any investment advisory contract . . . if such contract . . . (1) provides for compensation to the investment adviser on the basis of a share of capital gains upon or capital appreciation of the funds or any portion of the funds of the client.").

68. *See supra* notes 62-65 and accompanying text.

69. 15 U.S.C. § 80b-5(b).

70. Dodd-Frank Wall Street Reform and Consumer Financial Protection Act of 2010 § 418, 12 U.S.C. §§ 5481-5603 (2012).

clients to avoid registration,[71] but these provisions have since been rolled back considerably.[72]

Further, the sponsors can structure the governance of PPE Type 1 so that it may avail itself of the "controlled company" exception from certain stock exchange listing rules.[73] This exception allows PPE Type 1 to avoid certain requirements such as the requirement that all boards of directors of listed companies have a majority of independent directors and the requirement that all listed companies have a nominating and corporate governance committee that is composed entirely of independent directors.[74]

4. Examples from PPE Review

Eleven (not counting the three that are discussed under PPE Type 3) of the forty-two firms that I reviewed are PPE Type 1 firms.[75] I introduce here Oaktree Capital Group, LLC (Oaktree) as a representative example of a firm with the standard PPE Type 1 features described above in the foregoing Sections 1 through 3. Oaktree is a Delaware limited liability company and a holding company that controls all of the businesses and affairs of the "Oaktree Operating Group."[76] The "Oaktree Operating Group" refers to the group of limited partnerships through which Oaktree owns and controls the general partner and investment adviser of each of its funds.[77]

Oaktree is owned by its Class A and Class B unitholders.[78] All outstanding Class B units are held by an entity which is controlled by Oaktree's sponsors.[79] These Class B units represented, at the time of the IPO, 98.23% of the combined voting power of the outstanding

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71. *Id.* § 403.

72. On September 9, 2016, the House of Representatives passed H.R. 5424, the Investment Advisers Modernization Act of 2016, which, among other things, reduces the reporting obligations of investment advisers to private funds unless such investment adviser is a large hedge fund adviser or a large liquidity fund adviser (as such terms are defined in Form PF).

73. NEW YORK STOCK EXCHANGE, LISTED COMPANY MANUAL § 303A.00, Intro. (2018) ("A listed company of which more than 50% of the voting power for the election of directors is held by an individual, a group or another company is not required to comply with the requirements of sections 303A.01 [Independent Directors], 303A.04 [Nominating/Corporate Governance Committee] or 303A.05 [Compensation Committee].").

74. *Id.*

75. These companies are: Affiliated Managers Group, Inc., Compass Diversified Holdings, FORM Holdings Corp., Fortress Investment Grp - Cl A, KKR LP, Leucadia National Corporation, Oaktree Capital Group, LLC, Och-Ziff Capital Management Group, LLC, PJT Partners, Inc., The Blackstone Group LP, and The Carlyle Group LP.

76. Oaktree Capital (Form S-1), *supra* note 61, at 61.

77. *Id.*

78. *Id.* at 7.

79. *Id.* at 57.

Class A and Class B units.[80] As a result, the sponsors control Oaktree, the Oaktree Operating Group, and all funds managed thereby.[81]

Further, Oaktree's operating agreement provides that so long as its sponsors (or their successors or affiliated entities) collectively hold, directly or indirectly, at least 20% of the aggregate outstanding Oaktree Operating Group units (referred to as the "Oaktree control condition"), the manager entity, which is 100% owned and controlled by its sponsors, will be entitled to designate all of the members of Oaktree's board of directors.[82] So long as the Oaktree control condition is met, Class B units are entitled to ten votes per unit; if the Oaktree control condition is not satisfied, Class B units will be entitled to just one vote per unit.[83] During the time the Oaktree control condition is satisfied, Oaktree will not be required to hold annual meetings of unitholders.[84]

As of the date of the prospectus, the sponsors were entitled to approximately 50.05% of the economic returns of the Oaktree Operating Group.[85] Some of the sponsors' economic interests in the Oaktree Operating Group are held through entities other than the issuer, which may give rise to conflicts of interest.[86] As to conflicts that may arise between the interests of the sponsors and public investors in the issuer (the Class A unitholder), Oaktree's operating agreement contains language that makes it difficult for a Class A unitholder to challenge the resolution of any such conflicts of interest.[87] For example, the operating agreement provides that potential conflicts of interest may be resolved by outside directors even if such directors hold interests in Oaktree.[88] The operating agreement also contains provisions that substantially limit the remedies available to a Class A unitholder compared to those that would have been available if the company were a corporation.[89] Oaktree has also availed itself of the "controlled company" exemption from certain NYSE governance rules.[90]

Oaktree avails itself of many of the features described above as characteristics of Type 1 PPE. In this way, Type 1 PPE retains many private company-like features even after its decision to go public. As such, the primary concern of a public investor in PPE Type 1 is the

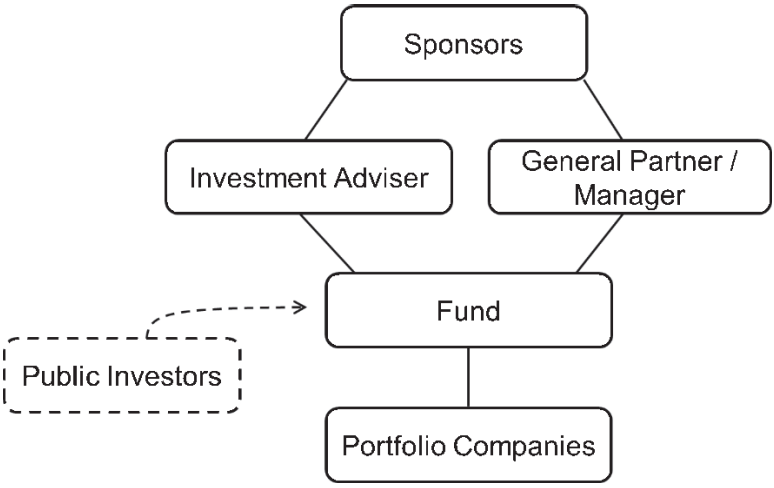
80. *Id.*
81. *Id.* at 57.
82. *Id.*
83. *Id.* at 10.
84. *Id.* at 152.
85. *Id.* at 46.
86. *Id.*
87. *Id.* at 46-47.
88. *Id.* at 46.
89. *Id.* at 47.
90. *Id.* at 7.

conflicts of interest that may arise between the public investor and controlling investors, and the role of organizational laws in mitigating such conflicts becomes paramount in PPE Type 1. The regulatory implications of this hybridity are explored in greater detail in Part IV.

B. PPE Type 2: Public-Private Equity Fund

Under this structure, the private equity fund is the entity whose shares are being offered to public investors. In this PPE type, the public investors are situated underneath and are subject to the advisement and management of the adviser and manager entities controlled by the sponsor.

Figure 3: PPE Type 2 (PPE Fund)



1. Structure

PPE Type 2 (or **PPE Fund**) is the entity that is directly engaged in making investments in portfolio companies in accordance with its investment objective and strategies. By investing in PPE Type 2, investors have the opportunity to invest in a portfolio of companies that are not otherwise available for general public investment. What the investor owns is its pro rata share of a portfolio of companies in which the fund invests and the returns generated thereby.

PPE Type 2 will use the proceeds from its public offering to make investments in its portfolio companies. Since returns from these investments are realized through a sale or public offering of the PPE Fund's portfolio companies, which may take a number of years, an investor in these PPEs may have to wait for some time for these realization events to materialize.

2. Governance

Typically, PPE Type 2 are organized as corporations, and their business and affairs are managed by the fund's board of directors. The board of directors is responsible for appointing officers and overseeing PPE Type 2's investment activities, asset valuations, financing arrangements, and corporate governance activities.

To the extent that the PPE Fund is one of many funds that are managed by the manager, the members of the manager's investment team may be faced with conflicts in the allocation of investment opportunities and payment of management fees among the different funds. Conflicts may be more severe when there are overlapping ownership interests between the fund and the adviser.

3. Regulation

PPE Funds commonly elect to be regulated as both a BDC under the Investment Company Act[91] and a regulated investment company (RIC) under Subchapter M of the Internal Revenue Code (the 'Code').[92]

BDCs are companies that primarily invest in companies with total assets of $4,000,000 or less and capital and surplus of $2,000,000 or less.[93] This election subjects PPE Type 2 to the governance requirements of the Investment Company Act[94] but offers relief from several key economic restrictions that are otherwise applicable to investment companies under the Investment Company Act, notably, leverage requirements.[95]

In order to maintain its qualification as an RIC under the Code, PPE Funds must meet applicable income source and distribution as well as asset diversification requirements specified in the Code.[96] Notably, PPE Funds are required to distribute 90% of their investment company taxable income back to their investors.[97]

In addition, in order to maintain its status as a BDC, 70% of the value of the total assets of PPE Type 2 must be invested in qualifying assets, as defined in the Investment Company Act.[98] The BDC regulatory regime provides preferential regulatory treatment to funds that

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91. 15 U.S.C. § 80a-53.

92. 26 U.S.C. §§ 851-852.

93. Investment Company Act Rule, 17 C.F.R. § 270.2a-46.

94. For example, PPE Funds are required to have a board of directors with at least 40% of its members being not "interested persons" (as that term is defined in section 2(a)(19) of the Investment Company Act. 15 U.S.C. § 80a-10).

95. 15 U.S.C. § 80a-18(f).

96. 26 U.S.C. § 851.

97. 26 U.S.C. § 851(b)(2).

98. 15 U.S.C. § 80a-54.

comply with the regulatory definitions of a BDC.[99] It should be noted however that the reason for regulatory relief is not connected to the characteristics of the *investor* in the PPE Fund but to the characteristics of the *investee* (i.e., the portfolio companies in which the PPE Fund invests).

4. Examples from PPE Review

Twenty-five (not counting the three that are discussed under PPE Type 3) of the forty-two firms I reviewed are PPE Type 2 funds.[100]

I use the example of Blackrock Capital Investment Corporation (formerly BlackRock Kelso Capital Corporation) to highlight the nature of conflicts and governance arrangements that arise between a PPE Fund and other entities within the private equity structure.

BlackRock Capital Investment Corp (BKCC) is an externally-managed, non-diversified, closed-end management investment company that has elected to be regulated as a BDC under the 1940 Act. As a BDC, PPE Funds must obtain stockholder approval to change the nature of their business so as to cease to be a BDC. However, it should be noted that certain principal investors of BKCC beneficially owned approximately 70.8% of the outstanding shares of the company's common stock at the time of its IPO.[101]

Furthermore, BKCC's adviser and certain entities that are under the adviser's management own shares of BKCC. Certain of the adviser entity's members and employees have negotiated the right to receive a number of shares of the issuer's stock if the performance of the stock exceeds certain thresholds.[102] In addition, the senior management and the chairman of the board of directors have ownership interests in the adviser entity (BlackRock Kelso Capital Advisors, LLC).[103]

The primary concern of a public investor in PPE Type 2 is the conflicts of interest that may arise between the public investor and

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99. 17 C.F.R. § 270.2a-46.

100. American Capital Ltd, Blackrock Capital Investment Corporation, Capital Southwest Corp, Capitala Finance Corp, Fidus Investment Corp, FS Investment Corp, FNFV Group, Garrison Capital Inc., Gladstone Investment Corp, Goldman Sachs BDC Inc., Golub Capital BDC Inc., GSV Capital Corp, Hercules Capital Inc., KCAP Financial Inc., Main Street Capital Corp, Medley Capital Corp, MVC Capital Inc., New Mountain Finance Corp, Pennantpark Investment Corp, Prospect Capital Corp, Safeguard Scientifics Inc., Solar Capital Ltd, TCP Capital Corp, THL Credit, Inc., and Triangle Capital Corp.

101. BlackRock Capital Investment Corp., Registration Statement of Small Business Investment Companies (Form N-2 Pre-Effective Amendment No.2) 27 (Jun 14. 2007) [hereinafter BlackRock Capital (Form N-2)], https://www.sec.gov/Archives/edgar/data/1326003/000119312507135385/dn2a.htm [https://perma.cc/9MZV-724F] ("[C]ertain of our principal investors . . . will beneficially own, in the aggregate, approximately 70.8% of the outstanding shares of our common stock.").

102. *Id.* at 71-72 (Certain relationships and transactions).

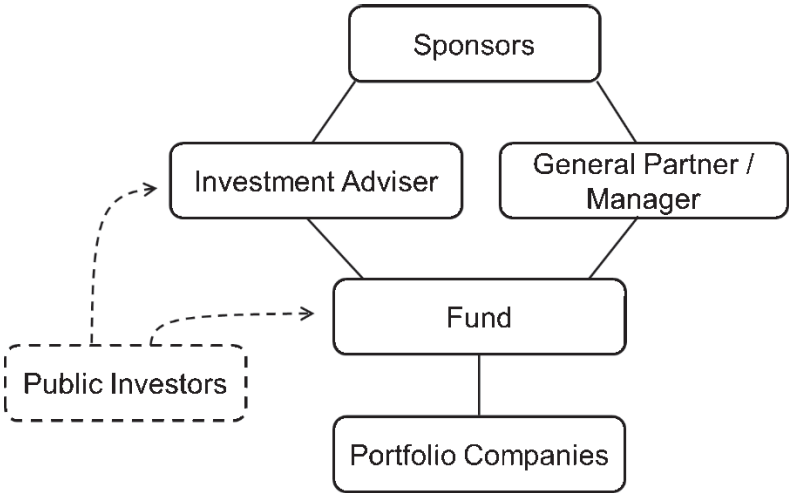
103. *Id.*

its adviser. The role of investment fund and investment adviser regulations in mitigating such conflicts therefore becomes paramount in PPE Type 2.

C. PPE Type 3: PPE (Manager and Fund) Combination

The PPE Types that have been reviewed thus far have occupied mutually exclusive spheres. BKCC is a PPE Fund with an investment adviser that is a private entity. Oaktree is a PPE Manager that advises and manages funds that draw investments from private investors. The third and last type of PPE that is discussed here is a PPE structure where both adviser and fund entities are offered for public investment.

Figure 4: PPE Type 3 (PPE Combination)



PPE Type 3 (or **PPE Combination**) is a combination of PPE Type 1 and PPE Type 2. It should be noted that PPE Type 3 may be comprised of multiple PPE Managers and PPE Funds and thus Figure 3 is only a simplified depiction of PPE Type 3. While the structural and governance features of the PPE Manager and PPE Fund that comprise PPE Type 3 are similar to the entities that were described in the previous Sections covering PPE Type 1 and PPE Type 2, I discuss PPE Type 3 as a separate structure because of its unique investor and regulatory implications. There are three pairs of PPE Type 3 firms in the forty-two PPE businesses that I reviewed.[104] I use the example of Ares Management, L.P. (ARES) and Ares Capi-

104. These pairs are: Apollo Global Management and Apollo Investment Corp; Ares Management, L.P. and Ares Capital Corp; and Fifth Street Asset Management Inc. and Fifth Street Finance Corp.

tal Corporation (ARCC) to illustrate the unique investor and regulatory concerns of PPE Type 3.

By way of background, ARES was established in 1997 by Antony Ressler, Michael Arougheti, David Kaplan, John H. Kissick, and Bennett Rosenthal (collectively, "Ares co-founders").[105] Immediately prior to the decision to go public, ARES was one of the most successful alternative asset management businesses, with approximately $74 billion of assets under management.[106] As noted in ARES' prospectus: "Over the past ten years, our assets under management and total management fees, which comprise a significant portion of our total fee revenue, have achieved compound annual growth rates of 31% and 33%, respectively."[107]

ARCC is a leading specialty finance company that provides debt and equity financing to private middle-market companies. Following its acquisition of American Capital, Ltd. (ACAS) on January 3, 2017,[108] ARCC became the largest BDC in terms of both market capitalization and total assets under management.[109] ARCC is externally managed by Ares Capital Management LLC, which is a subsidiary of ARES.[110]

1. Structure

ARES: On May 1, 2014, ARES launched its initial public offering, selling 11,363,636 common units, which began trading on the New York Stock Exchange under the ticker symbol "ARES."[111]

The common units offered to public investors represented limited partner interests in ARES. The proceeds of the offering were used to purchase newly issued Ares Operating Group units, to repay outstanding balances of the credit facility, for general corporate purposes, to fund growth initiatives, and to reimburse expenses of the offering.[112]

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105. *Ares Management L.P.*, WALL ST. J., http://quotes.wsj.com/ARES/company-people [https://perma.cc/VKK5-YPVN].

106. Ares Mgmt., L.P., Registration Statement (Form S-1) 1 (Mar. 31, 2014) [hereinafter Ares Mgmt. (Form S-1)], https://www.sec.gov/Archives/edgar/data/1176948/000104746914003231/a2219379zs-1.htm [https://perma.cc/G4BW-PTJC].

107. *Id.*

108. At the time I constructed the PPE universe (as of September 1, 2017) American Capital, Ltd. (ACAS) had not yet been acquired by ARCC and is counted in my sample as a PPE Fund under Section III.B.

109. *About Ares Capital*, ARES CAPITAL CORP., http://www.arescapitalcorp.com/about-ares-capital-corp [https://perma.cc/FJ84-9F96].

110. *Id.*

111. Ares Mgmt., L.P., Quarterly Report (Form 10-Q) 6 (June 10, 2014) [hereinafter Ares Mgmt. (Form 10-Q)], https://www.sec.gov/Archives/edgar/data/1176948/000104746914005478/a2220428z10-q.htm [https://perma.cc/G6N8-429Y].

112. *Id.* at 79.

The common units sold in the IPO represented 14.37% of the total number of common units outstanding, but only 5.48% of the voting power of ARES.[113] Immediately following the offering, the Ares co-founders had sufficient voting power to determine the outcome of matters submitted for a vote of unitholders.[114] The Ares co-founders also own and control Ares Voting LLC, an entity that holds a special voting unit, providing it with a number of votes on any matter submitted for a vote of common unitholders of ARES, which is equal to the aggregate number of Ares Operating Group units held by the limited partners.[115]

In addition, thirty-seven senior professionals owned common units of ARES representing approximately 19% of the total number of common units outstanding.[116] Furthermore, prior to the IPO, Ares Management, L.P. had entered into exchange agreements that provided holders of Ares Operating Group units the option to exchange such units for common units of ARES on a one-for-one basis.[117] Holders of such units include the Abu Dhabi Investment Authority and Alleghany (referred to collectively by Ares Management, L.P. as their "strategic investors").[118]

ARES also restricts ownership of its common units on the basis that it will be administratively advantageous for one of its direct subsidiaries (Ares Real Estate Holdings LLC) to be taxable as a real estate investment trust (REIT).[119] For this reason, ARES' partnership agreement prohibits any common unitholder from beneficially or constructively owning more than 7.5% of the number of all outstanding common units.[120]

ARCC: ARCC is a closed-end, non-diversified management investment company incorporated in Maryland.[121] ARCC launched its IPO on October 8, 2004, with proceeds to be used toward investment in portfolio companies in accordance with the investment objectives and

113. *Id.* at 77.

114. Ares Mgmt., L.P., Prospectus (Form 424B4) 224 (May 5, 2014) [hereinafter Ares Mgmt. Prospectus], https://www.sec.gov/Archives/edgar/data/1176948/000104746914004598/a2219983z424b4.htm [https://perma.cc/FW62-RFD3].

115. *Id.* at 89.

116. *Id.* at 224.

117. *Id.* at 20.

118. *Id.* at 10, 242.

119. *Id.* at 17.

120. *Id.*

121. Ares Capital Corp., Articles of Incorporation (Exhibit 99(A)) (Apr. 16, 2004), https://www.sec.gov/Archives/edgar/data/1287750/000104746904012712/a2134010zex-99_a.htm [https://perma.cc/Y5MQ-85EH].

strategies described in the prospectus.[122] ARCC's investment objectives are to generate current income and capital appreciation through debt and equity investments in private, middle-market companies.[123]

Public investors in ARCC are acquiring an interest in ARCC and not any other funds that are managed by Ares investment professionals. In fact, SEC rules limit ARCC's participation in co-investments (unless it is able to receive a favorable exemptive order from the SEC) with other Ares funds.

ARCC pays management and incentive fees and reimbursable expenses to its manager, Ares Capital Management LLC, which is a subsidiary of ARES, as described above.[124] Public investors in the common stock of ARCC thus invest on a gross basis and receive distributions on a net basis after fees and expenses.[125]

For this reason, ARCC's manager may have interests that differ from those of the public investors of ARCC, which gives rise to a conflict. For example, the investment adviser may have an incentive to induce portfolio companies to accelerate or defer interest or other obligations owed to ARCC from one calendar quarter to another in order to maximize its quarterly incentive fee that is based on income.[126]

In addition, ARCC's manager manages multiple investment funds.[127] While the company explains that they expect the efforts of Ares investment professionals in connection with other fund businesses will be synergistic with and beneficial to the affairs of ARCC, invariably, conflicts of interest will arise. There may be cases where the partners and investment committee of ARCC's manager will have obligations to investors of the other funds in which they serve as officers, directors, or principals that are adverse to the interests of ARCC.[128]

2. Governance

ARES: ARES is organized as a Delaware limited partnership. As a limited partnership, ARES is managed by its general partner, which is wholly owned by an entity owned and controlled by Ares co-founders.[129] Decisions of the general partner are made by its member

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122. Ares Capital Corp., Registration Statement (Form N-2) 1, 14 (June 21, 2016) [hereinafter Ares Capital Corp. (Form N-2)], https://www.sec.gov/Archives/edgar/data/1287750/000104746916013910/a2228956zn-2.ht.

123. *Id.* at 1-2.

124. *Id.* at 8.

125. *Id.* at 37.

126. *Id.*

127. *Id.* at 84.

128. *Id.* at 36.

129. Ares Mgmt. Prospectus, *supra* note 114, at 12 (Our Organizational Structure Following this Offering and the Offering Transactions).

(Ares Partners Holdco LLC), which is an entity owned and controlled by Ares co-founders. Each Ares co-founder sits on the board of managers of Ares Partners Holdco LLC so long as he is employed by the company and actively provides services.[130] Decisions by this board of managers are made by a majority of Ares co-founders.[131]

In addition, so long as the "Ares control condition" is satisfied (i.e., if the Ares co-founders and other Ares personnel hold 10% or more of the limited voting power), ARES' partnership agreement provides that its general partner will have no authority other than that which the member of the general partner chooses to delegate to it.[132] In the event the Ares control condition is no longer satisfied, the board of directors of the general partner will be responsible for the operations and activities of ARES.[133]

Common unitholders' voting rights are further restricted by a provision in ARES' partnership agreement stating that any common units held by a person that beneficially owns 20% or more of any class of common units then outstanding (excluding affiliates and approved transferees) cannot be voted on any matter.[134]

ARCC: Ares Capital Corporation's business and affairs are managed under the direction of its board of directors, which consists of five members, three of whom are not "interested persons" (as defined in section 2(a)(19) of the Investment Company Act).[135]

ARCC is organized as a Maryland corporation. Pursuant to Maryland's Control Share Acquisition Act, control shares of a Maryland corporation have no voting rights except to the extent approved by a vote of two-thirds of the votes entitled to be cast on the matter.[136] Maryland law also permits a Maryland corporation to include in its charter a provision limiting the liability of its directors and officers to the corporation and stockholders for money damages subject to enumerated exceptions.[137] ARCC's charter eliminates directors' and officers' liability to the maximum extent permitted by Maryland law.[138]

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130. *Id.* at 63 ("Ares Partners Holdco LLC is owned by our Co-Founders and managed by a board of managers, which is composed of our Co-Founders.").

131. *Id.* ("Decisions by the board of managers generally are made by a majority of the Co-Founders, which majority, subject to a minimum ownership requirement, must include Antony P. Ressler.").

132. *Id.* ("Our common unitholders do not elect our general partner or, except in limited circumstances, vote on our general partner's directors and will have limited ability to influence decisions regarding our businesses.").

133. *Id.* at 224.

134. *Id.* at 18-19.

135. Ares Capital Corp. (Form N-2), *supra* note 122, at 148.

136. MD. CODE ANN., CORPS. & ASS'NS §§ 3-701 et seq. (West 2017).

137. *Id.* § 2-405.1.

138. Ares Capital Corp. (Form N-2), *supra* note 122, at 198-99.

3. Regulation

ARES: Despite its impressive pre-IPO operating history, ARES is, pursuant to regulatory definitions, an "emerging growth company" (EGC), as that term is defined in the Jumpstart Our Business Startups (JOBS) Act.[139] As an EGC, ARES is eligible to take advantage of exemptions from various reporting requirements that are otherwise applicable to public companies.

ARES has also adopted modifications in its partnership agreement that allow its general partners to engage in transactions that might be prohibited by state law fiduciary duty standards.[140] By purchasing the common units, each public investor is treated as having consented to the provisions set forth in the partnership agreement.[141]

ARCC: Ares Capital Corporation elected to be regulated as a BDC under the Investment Company Act of 1940. Ares Capital Management LLC, a subsidiary of Ares Management, L.P. and an SEC-registered investment adviser, is the investment adviser to ARCC.

4. Summary

The foregoing discussion of ARES and ARCC as a representative example of PPE Type 3 is intended to show that ARES and ARCC, as standalone entities, resemble other PPE Managers and PPE Funds, respectively.

In the same way that the primary concern for PPE Type 1 was conflicts of interest between public investors and controlling investors, the most pertinent risk for a public investor in ARES is the mishandling of conflicts of interest that may arise between its interests, on the one hand, and the interests of the Ares co-founders, senior professionals, and strategic investors, on the other hand.

And in the same way that the primary concern for PPE Type 2 was conflicts of interest between public investors and the investors of the other funds managed by its adviser, the most pertinent risk for a public investor in ARCC is the mishandling of conflicts of interest that may arise between its interests, on the one hand, and the interests of the investors in the other funds in the Ares platform, on the other hand.

However, what is unique about PPE Type 3, and why it is discussed as a separate type of PPE, is that investors in these cases have the opportunity to invest in both the fund and manager entities should they wish to do so. In other words, public investors in PPE Type 3 have the ability to hedge against risks and diversify

139. Ares Mgmt. Prospectus, *supra* note 114, at 16.

140. *Id.* at 249-51.

141. *Id.* at 15.

their returns by investing in multiple layers of the same private equity structure. Then, the primary concern of the public investor in PPE Type 3 is whether they are provided with accurate and timely disclosures that will allow them to make an informed decision. The availability of a market alternative to address the risks associated with the individual components of PPE Type 3 prompt a reassessment of the regulatory priorities for PPE Type 3.

IV. MAPPING THE REGULATORY FRAMEWORK ONTO THE TYPOLOGY

There are some common features among all PPE that explain why and how they should be regulated differently from traditional private equity. First, investors in traditional private equity have relied on durational limits as a way to discipline the fund.[142] Traditional private equity funds are not perpetual in duration, and thus sponsors have to attract new capital every few years. This capital raising cycle tends to motivate high levels of fund performance. On the other hand, public investors in PPE are not locked into their investment for any period of time and, if dissatisfied, can sell their shares in the open market at any time.[143] For this reason, while the freedom of contract to negotiate the durational limits of investment is important for traditional private equity, in the PPE context, the focus is on the timing and content of disclosures to aid PPE investors in making the decision of whether or not to exit their investment.

Second, while traditional private equity draws large amounts of investments from a small number of investors, PPE draws varying amounts of investments from a large number of investors. For this reason, many exemptions that were available to traditional private equity because of the small number of investors, their wealth, and the private nature of offerings are no longer applicable to PPE.

While there are commonalities among them, PPEs as shown in Parts II and III are a diverse and heterogeneous segment. More importantly, PPEs issue shares to the public at every level of the private equity structure—the management company, investment company, or both. At the same time, PPE is an organization (i) with multiple owners and managers, (ii) that pools capital from multiple sources for investment in other enterprises, and (iii) that offers its securities to the public. As such, (i) organizational, (ii) fund / adviser, and (iii) securities regulatory regimes all apply.

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142. Masulis & Thomas, *supra* note 26, at 222.

143. Lee Harris, *A Critical Theory of Private Equity*, 35 DEL. J. CORP. L. 259, 275 (2010) ("Limited partnership investors' ability to constrain management's conduct by selling their interests in the firm is less realistic because the market for such interest is thin, with relatively few buyers and sellers.").

The result of this multiplicity has been the piling on of regulations, which may unintentionally create increased opportunities for regulatory arbitrage. As discussed in Part III, the usual levers used to control agency problems in large public corporations are generally unavailable in PPE Type 1. At the same time, contractual limits on voting and fiduciary duties are commonly observed. The guarantee of permanent capital that comes from PPE's public status could potentially dilute the efficiency of private equity governance, and the governor role of repeat, institutional owners may be limited when there is a conflict of interests among investors. Notably, the widespread use of devices like limited call rights and exchange agreements, which create gains for some investors at the expense of other investors, means there can be no expectation of fair treatment.

After noticing these gaps, the remainder of this Article matches each PPE type to the regulatory regime that is best equipped to manage these concerns. What I've shown from the discussion in Part III is that there are risks that are especially pertinent to each type of PPE. The primary concern of a public investor in PPE Type 1 is the conflicts of interest that may arise between the public investor and controlling investors, and the role of organizational laws in mitigating such conflicts becomes paramount in PPE Type 1. The primary concern of a public investor in PPE Type 2 is the conflicts of interest that may arise between the public investor and its adviser, and the role of investment fund and investment adviser regulations in mitigating such conflicts becomes paramount in PPE Type 2. Lastly, the primary concern of a public investor in PPE Type 3 is the accuracy of disclosures that will allow the investor to make an informed decision, and the role of securities regulation in facilitating such decisionmaking becomes paramount in PPE Type 3. This segmented view of the PPE universe facilitates the tailoring of regulations.

A. PPE as an Organization

1. Regulatory Overview

Organizational laws (e.g., corporate, partnership, LLC, and trust laws) regulate the internal organizational affairs of PPE. Substantive regulation of organizational affairs is seen as a subject for state regulation. As a result, when it comes to principles of corporate governance, the laws of the entity's state of organization are determinative.[144] The

144. Since it would be impossible to summarize the law for all entity types for all states, I use Delaware as the representative example. Delaware is the jurisdiction that is selected most frequently by PPE firms although a number of PPE have incorporated as (or converted to) Maryland entities. For a detailed study and comparison of the principal provisions of the Delaware and Maryland Corporation Statutes see James J. Hanks, Jr., *Com-*

specific provisions of organizational laws that relate to PPE include formation, issuance of securities, dividends, reorganizations, and the duties and responsibilities of directors and shareholders, among others.

Since the corporate form is the most frequently observed organizational choice among PPE, I will focus here on that regime. One of the functions of corporate law is to provide businesses with a legal form that possesses the core attributes desired by business corporations.[145] According to Henry Hansmann and Reinier Kraakman, these attributes are: legal personality, limited liability, transferability of shares, delegated management, and investor ownership. Under this view, the goal of corporate law is to offer a legal form that makes these core attributes widely accessible, efficient, and friendly for its users.[146]

Another function of corporate law is to constrain value-reducing opportunism.[147] Under this view, the goal of corporate law is to reduce the agency problems that arise from conflicts within the organization. According to Frank Easterbrook and Daniel Fischel, the law's role is to remedy the exploitative tendencies of managers by, for example, setting minimum voting rules and placing restrictions on managers.[148] Hansmann and Kraakman take a broader view, defining conflicts to cover conflicts not only between managers and shareholders, but also among shareholders and between shareholders and other constituents such as employees or creditors.[149]

Alternative forms to the corporate form are available, and a number of PPE are organized as partnerships, limited liability companies, and trusts. Some of the main considerations that drive the sponsor's choice of form and jurisdiction of organization when structuring private equity, as well as PPE, are tax treatment,[150] limited liability protection,[151] and the ability to waive fiduciary duties.[152]

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parison of the Principal Provisions of the Delaware and Maryland Corporation Statutes (2016), *in* THE INITIAL PUBLIC OFFERING LEGAL SOURCEBOOK (2d ed. 1998).

145. Hansmann & Kraakman, *supra* note 43, at 2 ("Self-evidently, a principal function of corporate law is to provide business enterprises with a legal form that possesses these five core attributes [of the business corporation].").

146. *Id.*

147. *Id.* ("[A] second, equally important function of corporate law . . . is, constraining value-reducing forms of opportunism among the constituencies of the corporate enterprise.").

148. EASTERBROOK & FISCHEL, *supra* note 47, at 1.

149. Hansmann & Kraakman, *supra* note 43 (describing the three principal conflicts with the corporation).

150. A partnership is a flow-through entity for federal income tax purposes; an LLC enjoys the same flow-through taxation as a partnership for federal income tax purposes but may be treated as a corporation for local tax purposes. JACK S. LEVIN & DONALD E. ROCAP, STRUCTURING VENTURE CAPITAL, PRIVATE EQUITY, AND ENTREPRENEURIAL TRANSACTIONS ¶ 1001 (2012) (discussing partnership versus corporate form for PE fund).

151. Limited liability is available to shareholders of a corporation, who will not be personally liable for a corporation's debts, unless the shareholder actually participated in the act that created the liability. An LLC is generally treated like a corporation for limited

2. *Regulating PPE as Organizations*

As discussed in Section III.A, the most pertinent risk for a public investor in PPE Type 1 is conflicts of interest between the public investor and insiders within the same entity. These risks are best addressed within the framework of organizational laws.

Even as private equity becomes public, PPE still retains many private company attributes. As such, not all PPE exhibit what corporate law scholars have deemed core attributes of a company. Since the goal of corporate law is to facilitate a corporate legal form desired by its users, the emergence of PPE requires a rethinking of *what* it is we are trying to facilitate.

In addition, the agency problems in PPE take new forms. The usual assumption that "investors of capital have . . . highly homogenous interests among themselves, hence reducing . . . the potential for costly conflict among those who share governance of the firm" does not hold in PPE.[153] Inter-investor conflicts arise in PPE because of the heterogeneous nature of investors' interests. Within the PPE universe, certain conflicts are more acute in some types than in others, which then requires a tailoring of efforts to mitigate conflicts of interests.

With respect to fiduciary duties, there remain open questions about the extent to which traditional corporate fiduciary duties may be waived and whether they should also apply to unincorporated entities. Delaware has been permissive on this topic. Delaware's partnership statute, and the LLC statute that tracks the partnership statute, state that: "A partnership agreement may provide for the limitation or elimination of any and all liabilities for breach of contract and breach of duties (including fiduciary duties)" and "a partner . . . shall not be liable . . . for breach of fiduciary duty for . . . good faith reliance on the provisions of the partnership agreement."[154]

The general policy underlying these fiduciary duty waivers is the respect for the freedom of contract, which presumes that the parties

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liability purposes. Delaware Limited Liability Company Act, 6 DEL. C. § 18-303(a). A general partner typically has unlimited liability for the partnership's liabilities, unless the general partner uses a limited-liability entity intermediary or the partnership qualifies as a limited liability partnership (LLP). Details about each of these strategies are outlined in LEVIN & ROCAP, *supra* note 150, ¶ 302.1.2 (Difficulties in Achieving GP Limited Liability). However, "piercing the veil" or statutory liability doctrines (e.g., CERCLA, ERISA) apply equally whether the entity is a corporation, partnership, or LLC.

152. LEVIN & ROCAP, *supra* note 150, ¶ 1001 (Partnership Versus Corporate Form for PE Fund).

153. John Armour, Henry Hansmann & Reinier Kraakman, *The Essential Elements of Corporate Law: What Is Corporate Law* 14 (Harv. Law Sch., Discussion Paper No. 643, 2009).

154. *See* Delaware Revised Uniform Partnership Act, 6 DEL. C. § 17-1101 (f) & (e); Delaware Limited Liability Company Act, 6 DEL. C. § 18-1101 (f) & (e).

have the capacity and opportunity to review and consent to the contract. Free will, consent, assumption of risk, and private autonomy are used to legitimize the unavailability of certain core rights. But even in the case of a Delaware partnership, certain duties are nonwaivable. For example, the partnership agreement of private equity partnerships may not limit liability for a bad faith violation of the implied contractual covenant of good faith and fair dealing.[155]

PPE Type 1 firms have succeeded at "going public" while "staying private." Incumbent owners of PPE Type 1 firms have used complex contracts and availed themselves of various legal and regulatory exceptions to retain most of the private benefits of private equity while spreading the risks and losses to new owners by taking their firms public.

Most critically, the control of the manager may be transferred to a third party and sponsors may sell their interests in the manager, in each case without unitholder consent.[156] Similarly, one tier of investors may have separately negotiated rights to exit from their investment upon the departure of key management personnel. In each of these cases, one group of investors are able to limit their exposure in a downturn by exiting before other groups without this advance notice opportunity.

Ronald Gilson and Charles Whitehead observe that a significant amount of interest in the primary offerings of "big name" private equity firms came from speculators and those who could not otherwise buy the underlying portfolio directly on more attractive terms.[157] It is accepted that investors who have paid more (or can otherwise offer more to the issuer) should enjoy preferential rights. However, it would be unrealistic in these cases to rely on such investors to play a governing role to discipline the issuer on behalf of all investors, especially in cases where the conflict to be resolved arises between the institution and public investors.

This view of sophisticated investors' presence as an indication that more protection of unsophisticated investors is needed goes against the current grain of scholarship and legislation.[158] Current scholarship has been focused on the governance role of sophisticated investors, especially institutional investors.[159]

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155. *See* Delaware Revised Uniform Partnership Act, 6 DEL. C. § 17-1101(c)-(f); Delaware Limited Liability Company Act, 6 DEL. C. § 18-1101 (c)-(f).

156. Oaktree Capital (Form S-1), *supra* note 61, at 47-48.

157. Gilson & Whitehead, *supra* note 8, at 258-59 n.134.

158. *See, e.g.*, Merritt B. Fox, *Retaining Mandatory Securities Disclosure: Why Issuer Choice Is Not Investor Empowerment*, 85 VA. L. REV. 1335 (1999).

159. The recently passed JOBS Act, for example, increases the number of record shareholders that triggers securities regulation to 2,000 with the caveat that there are no more than 499 non-accredited investors. JOBS Act, Pub. L. No. 112-06 § 501, 126 Stat. 306,

The missing lever in PPE Type 1 structure is that the general partner (GP) of PPE Type 1, if it is organized as a limited partnership, has severely constricted its fiduciary duties to unitholders.[160] Specific waivers of fiduciary duties vis-à-vis common unitholders have been entered into by contract.[161] For example, some GPs of PPE Type 1s have the right to make certain decisions in their sole discretion, which is defined to mean that the GP may consider any interests and factors, including its own interest (i.e., in its individual capacity). Any such decision made by the GP in its individual capacity and not in its capacity as GP will be "without any fiduciary obligation to [the limited partners] or the common unitholders whatsoever."[162]

As described at the outset, the goals of organizational laws are twofold. The first is to make available and facilitate the development of organizational forms that are desired by businesses, and the second is to mitigate conflicts of interest that arise within organizations. These two goals sometimes work in unison and other times in tension with one another. They are in tension when, for example, PPE sponsors may desire a full waiver of all personal liability arising from the enterprise. But organizational law—even the most permissive Delaware partnership statute—places limits on the sponsors' ability to waive their liability for acts that constitute a bad faith violation of the implied contractual covenant of good faith and fair dealing.[163] On the other hand, and in most cases, organizational law merely sets the starting point, allowing parties nearly full freedom to take as many steps in any direction from that starting point as they wish. As an example, although one standard feature of organizations is that owners of the

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325 (2012) (codified at 15 U.S.C. § 78l(g)(1)(A)); Langevoort & Thompson, *supra* note 38, at 365 ("This is a bow to the idea that such investors should protect themselves in terms of information rights, but the number of shareholders is then capped at 1,999, so that the idea cannot be taken to the extreme of an unlimited "sophisticated" shareholder base that never triggers 1934 Act registration.").

160. Oaktree Capital (Form S-1), *supra* note 61, at 185-86.

161. The decision and manner in which fiduciary duties are waived to the fullest extent in PPE is consistent with the empirical findings of legal scholars who have studied publicly-traded limited partnerships and limited liability companies. *See* Suren Gomtsian, *The Governance of Publicly Traded Limited Liability Companies*, 40 DEL. J. CORP. L. 207, 234-37 (2015) (finding that the majority of the 20 entities reviewed contain limits on fiduciary duties of care and loyalty); Mohsen Manesh, *Contractual Freedom Under Delaware Alternative Entity Law: Evidence from Publicly Traded LPs and LLCs*, 37 J. CORP. L. 555, 558 (2012) (finding that the majority of the 85 entities reviewed contain waiver or elimination of fiduciary duties without substitute mechanisms); Sandra K. Miller, *A New Direction for LLC Research in a Contractarian Legal Environment*, 76 S. CAL. L. REV. 351 (2003) (observing few contractual protections of minority shareholders); *cf.* Michelle M. Harner & Jamie Marincic, *The Naked Fiduciary*, 54 ARIZ. L. REV. 879 (2012) (finding non-uniformity across the 129 non-listed entities reviewed).

162. The Blackstone Group L.P., Registration Statement (Form S-1) 183 (Mar. 22, 2007) [hereinafter Blackstone (Form S-1)], https://www.sec.gov/Archives/edgar/data/1393818/000104746907002068/a2176832zs-1.htm [https://perma.cc/T59G-2RC3].

163. *See* Delaware Revised Uniform Partnership Act, 6 DEL. C. § 17-1101(c)-(f).

organizations have the right to vote, there is no rule which prohibits an issuer from issuing only non-voting stock to its stockholders, should it so choose.[164]

As PPE expands the private equity investment opportunity to public investors whose interests are not as well protected by contractual means, the agency-cost reducing role of organizational law becomes increasingly important and more limits on the facilitative nature of organizational laws may become appropriate.

B. PPE as Fund Structures

1. Regulatory Overview

1940 Act. Why do we have a separate regulatory regime for investment companies? The express function of investment company regulation is to regulate firms that hold investment securities that have been purchased with other people's money. An implicit function of fund regulation is to regulate a particular kind of agency relationship or organizational structure that is associated with such firms.[165] Both functions stem from the observation that firms that invest primarily in securities and manage assets on behalf of others are particularly susceptible to irresponsible management and unfair treatment of investors, therefore requiring special regulatory treatment.

Under the Investment Company Act, "investment company" is defined as any company that pools the investment of a number of investors into a fund that engages in the investment of securities.[166] A "company" is defined in section 2(a)(8) of the Act as "a corporation, [] partnership, [] association, [] joint-stock company, [] trust, [] fund, or any organized group of persons whether incorporated or not."[167] So, unless a private equity fund can find an applicable exemption, it will be an investment company that is subject to the 1940 Act's regulatory provisions.

Funds that are treated as a BDC under the 1940 Act may qualify as a RIC for federal income tax purposes. If the fund is an RIC under Subchapter M of the U.S. Internal Revenue Code of 1986 (the 'Code'), it will not be required to pay corporate-level income tax on its investment income.[168] As a RIC, the fund is required to distribute sub-

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164. Easterbrook and Fischel give the example of Ford, which issued non-voting stock so that it could keep company in the family's hands. EASTERBROOK & FISCHEL, *supra* note 47, at 13.

165. Morley, *supra* note 27, at 1279-81 (explaining the core function of the Investment Company Act of 1940).

166. 15 U.S.C. § 80a-3(a)(1)(A).

167. 15 U.S.C. § 80a-2(a)(8).

168. 26 U.S.C. §§ 851-852.

stantially all (i.e., at least 90%) of its income to shareholders. In addition, RICs must diversify their holdings within percentage limits specified in the Code.[169]

In addition to the BDC regime, funds may also seek to be licensed by the Small Business Administration ("SBA") as a small business investment company ("SBIC") under section 681(c) of the Small Business Investment Act of 1958.[170] SBICs refer to businesses that make loans, invest in equity securities, and provide consulting and advisory services to eligible small businesses. The SBA guarantees debentures of SBICs in amounts up to twice the amount of privately-raised funds of the SBIC.

Advisers Act. Why do we have a separate regulatory regime for fund advisers?[171] The purpose of fund adviser regulation is to protect the clients of an investment adviser (which, in the case of private equity firms, would be the funds organized by the sponsors).[172] The Advisers Act regulates the sponsors and advisers of investment funds and requires them to register with and be regulated as an investment adviser by the SEC unless they fall under an exemption.[173] Advisers to private equity funds fall squarely under the definition of "investment adviser" under the Advisers Act and are required to register as such unless exemptions apply.[174]

Some advisers to private equity funds are exempt altogether from registration requirements and from being regulated by the provisions of the Advisers Act (including the fee limitations described above under Part III.A.3). There are three exemptions that are the most frequently used by advisers to private equity funds: first, is as an investment adviser solely to private funds that has less than $150 million in assets under management; second, is as an investment adviser that is regulated as an adviser in the state where it has its principal office and has less than $25 million in assets under management; and third, is an investment adviser that does not advise any 1940 Act-registered investment companies.[175]

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169. *Id.*

170. 15 U.S.C. § 681(c).

171. The Investment Advisers Act of 1940 was originally enacted as Chapter 686, Title II, sections 201-244, and is now codified as 15 U.S.C. §§ 80b-1 et seq.

172. 15 U.S.C. § 80b-1.

173. 15 U.S.C. § 80b-3. An investment adviser that is not registered with the SEC may be required to register with the state where its principal place of business is located (blue sky laws).

174. 15 U.S.C. § 80b-2(a)(11).

175. *See* Investment Advisers Act of 1940, Pub. L. No. 114-94, § 203A (2015) (as amended).

2. Regulating PPE as Funds

As discussed in Section III.B, the most pertinent risk for a public investor in PPE Type 2 is conflicts of interest between the public investor and investors in other funds managed by the same investment adviser. These risks are best addressed within the framework of fund and adviser regulations.

Most PPE Type 2s have elected to be regulated as both a BDC under the Investment Company Act and a RIC under Subchapter M of the Code. A number of PPE Type 2s limit their investments to small businesses to avail themselves of the SBA guarantees. This subjects PPE Type 2 to the governance requirements of the Investment Company Act (such as section 2(a)(19), which requires the majority of PPE Type 2's board of directors to be "noninterested" persons and places severe restrictions and regulations on the relationship between the BDC and its investment adviser) but relieves PPE Type 2 from several key economic restrictions otherwise applicable to investment companies under the Investment Company Act (notably, leverage requirements).[176]

Generally, to be eligible to elect BDC status, a fund must furnish capital to companies that do not have access to conventional financing channels.[177] At least 70% of a BDC's total assets must be invested in eligible investments and assets that include non-listed and smaller cap companies.[178]

In addition to providing capital, BDCs must also offer significant managerial assistance to their portfolio companies,[179] which may take the form of guidance and counsel over the management, operations, or business objectives and policies of the portfolio companies, or exercising a controlling influence over the management of the portfolio companies.[180] This definition closely tracks the private equity model of ownership, except that the definition only requires that an offer, and not the actual provision, of managerial assistance be made. And, in the case where multiple BDCs are acting together in a deal, a BDC

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176. 15 U.S.C. § 80a-18(f).

177. Investment Company Act of 1940, Pub. L. No. 76-768, § 2(a)(46), 123 Stat. 2059 (as amended in 2009).

178. Even the remainder of BDC's assets must still be invested in a manner that is consistent with the purpose of a BDC. *See* Definition of Eligible Portfolio Co. Under the Inv. Co. Act of 1940, Release No. 27538 (Nov. 30, 2006) (codified at 17 CFR § 270.2a-46 & 17 CFR § 270.55a-1 (2007)) ("Congress did not specifically regulate how a BDC should invest the remainder of its assets ('30% basket') Congress clarified, however, that a BDC would be required to invest its 30% basket in a manner consistent with the overall purpose of SBIIA." (citations omitted)), https://www.sec.gov/rules/final/2006/ic-27538.pdf [https://perma.cc/Q8M2-PVTY].

179. Investment Company Act of 1940, Pub. L. No. 76-768, § 2(a)(47).

180. 15 U.S.C. § 80a-2(a)(47).

can meet this requirement so long as any person in the group makes available such managerial assistance.[181]

Other sections of the Investment Company Act govern the various operational elements of BDCs including the board of directors, related party transactions, leverage, valuation, code of ethics, fidelity bond requirements, indemnification, compliance programs, disclosure controls and procedures and internal control over financial reporting.

The BDC, RIC, and SBA regimes can best be summarized as regimes that relax certain regulatory levers or provide perks to private equity funds that stimulate the flow of capital and offer advisory services to businesses without access to traditional financing channels. This regulatory treatment recognizes the value that private equity strategies could bring to these firms and the subsequent value that such firms could add by creating jobs and revitalizing the economy.

Such positive externalities must, however, be balanced against the primary goals of fund regulation, which, as stated at the outset of this Section, are to foster responsible management and fair treatment of the funds' investors. As PPE expands the private equity investment opportunity to public investors, the weight placed on these primary rationales for fund regulation becomes more elevated.

C. PPE as Securities

1. Regulatory Overview

1933 Act. Why do we regulate the offering of securities? The purpose of the 1933 Act is to provide full and fair disclosure of the character of securities sold and to prevent fraud in the sales of securities.[182] The main function of the 1933 Act is investor protection, through mandated disclosure, with transparency as the dominant regulatory objective.[183] In particular, the focus is on the protection of public investors. The Supreme Court has described disclosures and other protections of the 1933 Act as not being needed for those investors who could "fend for themselves."[184]

All issuers of securities are required to provide detailed disclosures relating to the issuer and the securities, but private equity businesses have availed themselves of the various exemptions avail-

181. This is how specialty finance companies can also operate as a BDC by partnering with a private equity fund that offers significant managerial assistance.

182. *See, e.g.*, SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 186 (1963); Wilko v. Swan, 346 U.S. 427, 431 (1953); SEC v. Sw. Coal & Energy Co., 624 F.2d 1312, 1318 (5th Cir. 1980).

183. Langevoort & Thompson, *supra* note 38, at 338 ("Markets are increasingly fragmented and often opaque, even as transparency has become the dominant regulatory objective . . . .").

184. SEC v. Ralston Purina Co., 346 U.S. 119, 125 (1953).

able under section 4 of the 1933 Act. These exemptions include transactions that do not involve any public offering and the private placement exemption contained in SEC Regulation D's operative safe harbor exemptions.[185]

1934 Act. Why do we regulate public companies differently from their private counterparts? The purpose of the 1934 Act is to regulate securities exchanges and over-the-counter markets and to prevent inequitable and unfair practices on those exchanges and markets.[186]

The question of when a private enterprise should be forced to take on public status has significant legal and cost implications. Section 12(g) of the 1934 Act specifies the issuers that are required to register their securities with the SEC.[187] A 1934 Act reporting company is subject to the registration requirements and other regulations of the 1934 Act and must file annual reports on Form 10-K, quarterly financials on Form 10-Q, current reports on material developments on Form 8-K, and annual proxy statements, among others.[188]

2. Regulating PPE as Securities

As discussed in Section III.C, the most pertinent risk for a public investor in the various entities that comprise PPE Type 3 is the quality and timing of disclosures. These concerns are best addressed within the framework of securities regulation. The key component that is relevant to evaluating PPE as a public company is the timing and identity of the PPE entity that decides to engage in an IPO and list its shares on an exchange. In this way, the public investors' point(s) of entry in the PPE structure is relevant to determining the quality and content of the security and disclosures that are required to be made.

To start, the main features that applicable laws and regulations have been focused on when regulating private equity and PPE have been the size of the fund (i.e., total dollar amount of assets under management) and the representative investor of the fund. This makes sense when private equity pools only from sophisticated investors and the main regulatory focus is on the spillover and systemic risk implications of private equity and other funds on the broader financial markets.

But because PPE interfaces with public investors directly, even small funds and even those with only a few public investors are susceptible to conflicts and mismanagement that trigger regulation. The

185. 15 U.S.C. § 77d.

186. The Securities Exchange Act of 1934 was originally enacted as Chapter 404, sections 1-39, and is now codified as 15 U.S.C. §§ 78a-78pp.

187. 15 U.S.C. § 78l(g).

188. 15 U.S.C. § 78l(b).

opportunity to invest alongside sophisticated investors may well be what public investors want and explains why many have celebrated PPE as a welcome expansion and leveling of the investment playing field. But even in that case (or perhaps especially so in this case, since it means PPE is a product that public investors will actively invest in), regulatory backstops and protections should operate in the ways in which they were originally intended.

Yet another challenge of the well-known private equity players' IPOs is that the historical performance results are not necessarily indicative or relevant to the future results that public investors should expect from their investment. Yet, in the prospectus, the issuer presents information relating to the historical performance of the funds on a consolidated basis. For the manager entity in PPE Type 3, the value of assets and liabilities recognized in the pre-IPO financial statements remain unchanged when carried forward into the post-IPO financial statements because the sponsors of the pre-IPO business continue to control the post-IPO business.[189] As a result, the predecessor's financial statements are used as the post-IPO entity's historical financial statements.

For this reason, PPE Type 3 may be a good candidate for the "seasoning period" Adam Pritchard recommends in a recent article. The proposed seasoning period allows the market to process information about a new issuer prior to any public offering and may be appropriate for issuances by well-known private equity sponsors that have a rich operating history but no history operating under the proposed post-IPO structure.[190] In each case, it would be helpful for the public investor to understand what she is getting relevant to other investors based on an example of prior years, using the seasoning period as a way for PPE to reset its track record under the business model that is more pertinent to the public investor.

PPEs are companies that have launched a 1933 Act registered public offering and whose shares are listed on a national securities exchange, subjecting them to the requirements of the 1934 Act. The SEC, however, has the power to exempt certain issuers under its exemptive authority pursuant to section 14A(e) of the Exchange Act. For example, emerging growth companies (EGCs), as defined under the JOBS Act, enjoy a host of reduced disclosures, and some PPEs have availed themselves of EGC status.[191]

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189. *See* Oaktree Capital (Form S-1), *supra* note 61, at 60.

190. A. C. Pritchard, *Revisiting* "Truth in Securities" Revisited*: Abolishing IPOs and Harnessing Private Markets in the Public Good*, 36 SEATTLE U. L. REV. 999 (2013).

191. The JOBS Act eases some of the public company requirements (such as the requirement of an auditor assessment of a company's internal controls) for emerging growth companies. A subset of 1934 Act obligations will not apply for five years, subject to reve-

As private equity funds invest in private companies, there is no publicly available information about the portfolio companies in which the funds invest. Investors of the fund entity in PPE Type 3 must rely on the valuations performed by the agents of the fund. Private equity and PPE are particularly susceptible to valuation problems.

Recently, Fifth Street Finance Corp. (a publicly-listed BDC) and its investment adviser, Fifth Street Asset Management (FSAM) (also publicly-listed), were named as defendants in various legal proceedings.[192] The central claim brought against Fifth Street Finance Corp. was the mismanagement of Fifth Street Finance Corp. to boost the valuation of FSAM when it went public in 2014.

Fifth Street Finance Corp. entered into settlement agreements, which call for a payment of $14,050,000 (99% of which will be paid from insurance coverage). The proposed settlement of the shareholder derivative actions provides for waiver of fees charged by a Fifth Street affiliate to Fifth Street Finance Corp. for ten consecutive quarters and committing to a previously announced decrease in the base management fee from 2% to 1.75% for at least four years.[193]

While Fifth Street insiders may have been able to shortchange some of their investors at times, the ultimate resolution was one that benefitted all investors of the publicly-traded securities across the Fifth Street platform. Investors and regulators were able to advocate and bargain for the fee structure and governance changes they desired.

The proposed settlement includes certain governance and oversight enhancements, including provisions relating to equity ownership by board members, disclosure of executive compensation, director independence, valuation policies and processes, creation of a credit risk and conflicts committee, and increased consultation with outside advisers and independent third parties.[194] FSAM also entered into an agreement to settle its securities class action with a payment of $9,250,000. [195]

The key takeaway is that PPE picks and chooses from a menu of economic, financial, governance, and regulatory attributes in ways

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nues / market capitalization tests. JOBS Act, Pub. L. No. 112-106 § 101, 126 Stat. 306, 307 (2012).

192. In re Fifth Street Fin. Corp. Sec. Litig., No. 15-cv-7759 (LAK) (S.D.N.Y. 2016); In re Fifth Street Fin. Corp. S'holder Derivative Litig., No. 3:15-cv-01795-RNC (N.D. Cal. 2016); Ronald K. Linde v. Fifth Street Asset Mgmt. Inc., No. 1:16-cv-01941 (LAK) (S.D.N.Y. 2016); Verified Consolidated Amended Stockholder Derivative Complaint, In re Fifth Street Fin. Corp. Stockholder Litig., C.A. No. 12157-VCG, 2016 WL 3365291 (Del. Ch. June 15, 2016).

193. Fifth Street Fin. Corp., Current Report (Form 8-K) (Aug. 4, 2016) [hereinafter Fifth Street Fin. Corp. (Form 8-K)], https://www.sec.gov/Archives/edgar/data/1414932/000114420416116399/v446026_8k.htm [https://perma.cc/2R7P-LWTU].

194. *Id.*

195. *Id.*

that situate it all over the map. PPE are hybrid organizations that combine the liquidity benefits of going public with the private benefits of private company governance. PPE alters previously-held assumptions about both publicly-held firms and private equity, and there is a high degree of customization in PPE. Ignoring the heterogeneity across the PPE universe may be the source of some regulatory gaps.

With the goal of organizing the universe across the dimensions that regulations care most about, I use the investor's point of investment in the private equity structure as a way to meaningfully sort through the PPE universe and their regulation. Here, I have divided the forty-two PPE into those that offer to investors a share of the adviser / manager, fund, or both. Each group will of course contain a diverse set of issuers, but the three-part simplification helps investors understand the distinct investment opportunities and allows regulators to take the view of the investors that the regulations seek to protect.

V. CONCLUSION

Traditional private equity draws large investments from a small number of investors with the promise of delivering high levels of returns to their investors using innovative governance structures and investment strategies. And in large part, these innovations were achievable because the managers of private equity firms and funds were able to operate without the control and interference by fund investors, who relied on non-legal levers such as reputation and market power to protect themselves from managerial misconduct.[196] But what happens when public investors enter the picture? The decision of a number of private equity firms and funds to go public has prompted this question and is the motivation of this Article.

One positive outcome of this recent development has been the expanded availability of private equity innovations to the public investors. However, innovation can also breed investor and regulatory confusion. This Article offers a typology to segment the PPE universe according to whether the public investor is purchasing a share of the private equity adviser, fund, or both.

The typology looks at PPE from the perspective of the public investor and its relative position within the PPE structure. This Article also identifies the core functions of the multiple regulatory frameworks that apply, and which are sometimes in tension, and offers a segmented analysis of PPE that reflects this regulatory multiplicity. The analytical components that are relevant to evaluating PPE are

196. *See* Drury, III, *supra* note 10, at 84-86.

first, the structural and governance arrangements regarding ownership and control, and second, the nature and extent of conflicts of interest that arise therefrom. In this Article, I have shown that there is significant variety within the PPE segment on each of these dimensions and developed a typology that can be a useful sorting mechanism to examine the perils that each of the organizational, fund, and securities regulatory regimes care most about.

The typology can be used to design more tailored approaches to regulation that match each regulatory apparatus to its intended function. It can also be used to reevaluate existing regulatory efforts to engage in such tailoring. This review of PPE can also be used to generate new perspectives on the substantive doctrines and persistent debates in corporate law such as the desirability of investor passivity, the corporate democracy myth, and the contractual limits on waivers of the fiduciary duty of loyalty.[197] The overlapping roles of fiduciary doctrine, investor sophistication, and contract law in this area set up a robust research agenda for the future.

197. The operative question being: should corporate law rules be enabling (i.e., corporations are free to opt out) or mandatory (i.e., corporations would be limited from opting out)? *Compare* Lucian Arye Bebchuk, *Foreword—The Debate on Contractual Freedom in Corporate Law*, 89 COLUM. L. REV. 1395 (1989), *and* Robert C. Clark, *Contracts, Elites, and Traditions in the Making of Corporate Law*, 89 COLUM. L. REV. 1703 (1989), *with* Frank H. Easterbrook & Daniel R. Fischel, *The Corporate Contract*, 89 COLUM. L. REV. 1416 (1989).

APPENDIX

Active PPE Firms (U.S.)[198]

Company Name	Ticker	Stock Exchange	Market Capitalization (millions)
Affiliated Managers Group, Inc.	AMG	NYSE	$8,060.00
American Capital, Ltd.	ACAS	NASDAQ	$3,790.00
Apollo Global Management, LLC	APO	NYSE	$6,190.00
Apollo Investment Corp.	AINV	NASDAQ	$1,157.92
Ares Capital Corp.	ARCC	NASDAQ	$4,366.28
Ares Management, LP	ARES	NYSE	$2,870.00
BlackRock Capital Investment Corp.	BKCC	NYSE	$678.53
Capital Southwest Corp.	CSWC	NASDAQ	$218.82
Capitala Finance Corp.	CPTA	NASDAQ	$175.15
Compass Diversified Holdings	CODI	NYSE	$803.64
Fidus Investment Corp.	FDUS	NASDAQ	$233.53
Fifth Street Asset Management, Inc.	FSAM	NASDAQ	$149.81
Fifth Street Finance Corp.	FSC	NASDAQ	$722.76
Fidelity National Financial, Inc.	FNFV	NYSE	$912.51
FORM Holdings Corp.	FH	NASDAQ	$32.40
Fortress Investment	FIG	NYSE	$1,867.54
FS Investment Corp.	FSIC	NYSE	$2,039.91
Garrison Capital, Inc.	GARS	NASDAQ	$202.78
Gladstone Investment Corp.	GAIN	NASDAQ	$212.50
Goldman Sachs BDC, Inc.	GSBD	NYSE	$852.70
Golub Capital BDC, Inc.	GBDC	NASDAQ	$853.42
GSV Capital Corp.	GSVC	NASDAQ	$113.99
Hercules Capital, Inc.	HTGC	NYSE	$815.80

198. As of September 1, 2017.

Company Name	Ticker	Stock Exchange	Market Capitalization (millions)
KCAP Financial, Inc.	KCAP	NASDAQ	$109.82
KKR & Co., L.P.	KKR	NYSE	$10,490.00
Leucadia National Corp.	LUK	NYSE	$8,600.92
Main Street Capital Corp.	MAIN	NYSE	$1,500.24
Medley Capital Corp.	MCC	NYSE	$327.26
MVC Capital, Inc.	MVC	NYSE	$162.78
New Mountain Finance Corp.	NMFC	NYSE	$808.09
Oaktree Capital Group, LLC	OAK	NYSE	$7,050.00
Och-Ziff Capital Management Group, LLC	OZM	NYSE	$1,417.91
Pennantpark Investment Corp.	PNNT	NASDAQ	$426.89
PJT Partners, Inc.	PJT	NYSE	$500.10
Prospect Capital Corp.	PSEC	NASDAQ	$2,589.58
Safeguard Scientifics, Inc.	SFE	NYSE	$252.98
Solar Capital, Ltd.	SLRC	NASDAQ	$728.81
TCP Capital Corp.	TCPC	NASDAQ	$668.77
The Blackstone Group, L.P.	BX	NYSE	$32,300.00
The Carlyle Group, L.P.	CG	NASDAQ	$5,120.00
THL Credit, Inc.	TCRD	NASDAQ	$327.71
Triangle Capital Corp.	TCAP	NYSE	$617.02