

An Overview of GP-Led Secondary Transactions & Continuation Funds

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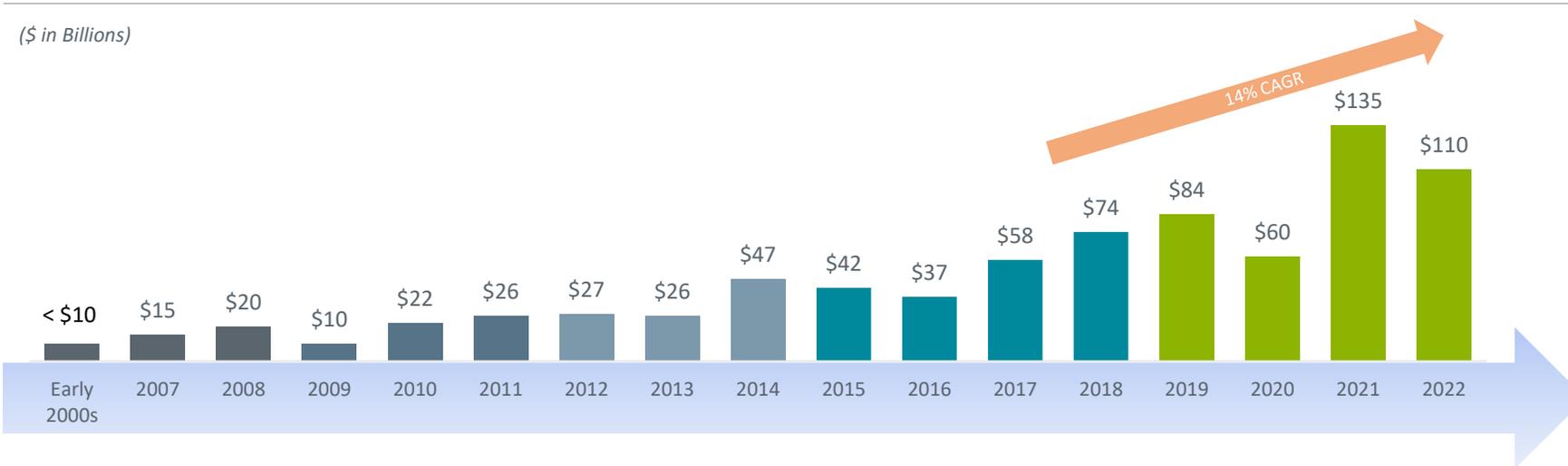
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Evolution of the Secondary Market

The GP-led secondary market today is driven by transactions on concentrated, high-performing portfolios with high-quality sponsors and strong go-forward alignment

SECONDARY MARKET TRANSACTION VOLUME



Early Secondary Market

- > Cottage industry with limited transaction volume and scope
- > Transaction volume driven almost exclusively by LP portfolio sales
- > Negative stigma associated with selling

Post-GFC and Eurozone Crisis

- > Increased secondary activity mostly centered around LPs seeking to address various liquidity and regulatory considerations
- > Large LP portfolio transactions become more common with multiple \$1BN+ sales occurring

Broader acceptance of the secondary market as a portfolio management tool for LPs

- > Investor appetite for secondaries grows allowing secondary investors to scale their franchises meaningfully
- > Early days of GP-led market predominately around tail-end funds

Fund restructurings for legacy "zombie funds" become more commonplace

- > Growing market acceptance around the benefits of these transactions to provide liquidity and realign economic incentives
- > LP portfolio market continues growth, driving overall volume

Innovation around transaction structure and scope drives widespread adoption of GP-led technology

- > Expansion to highly concentrated portfolios including single-asset continuation funds following the COVID-19 pandemic
- > Blue-chip sponsors utilize the market to provide optional liquidity to LPs while retaining trophy assets

- Rise of GP-led Transactions
- Maturity of Secondary Markets

Source: PJT Park Hill FY 2022 survey of leading secondary investors, PJT ongoing market research and publicly available industry data. Although information included above has been obtained from sources believed to be reliable, PJT Partners does not guarantee its accuracy or completeness.

Introduction & History of GP-Led Secondary Transactions

- **PE funds are illiquid, closed-ended vehicles with fixed offering periods and terms**
 - Existing LPs cannot liquidate their interests until the end of the fund's life (typically 10+ years)
 - New LPs cannot be admitted after the fund's offering period (typically first 12-18 months; typically before the fund begins investing)
 - GPs need to consider the fund's long-term capital needs; mature funds may not have sufficient time or capital to maximize portfolio company values
- **The secondaries market offers solutions for LPs, buyers and GPs:**
 - **Sellers**
 - Address liquidity needs
 - Rebalance portfolio
 - **Buyers**
 - Ability to diligence portfolio before investing
 - Shorter hold periods
 - Fund interests typically sell at a discount
 - **GPs**
 - Obtain fresh capital for follow-on investments
 - Extend time horizon to maximize value
 - Accelerate liquidity for existing LPs while establishing new relationships with strategic investors

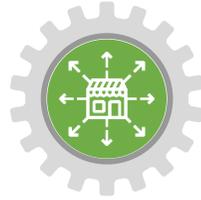
Introduction & History of GP-Led Secondary Transactions

- **Traditional (LP-initiated) secondary transactions**
 - “Plain vanilla” sale of LP interest in one fund
 - Portfolio sales
 - More complex flavors: deferred consideration; derivative secondaries; synthetic transactions; leveraged/secured portfolios as collateral
- **GP-led secondary transactions**
 - Fund restructurings
 - Strip sales
 - Annex / top-up funds
 - Tender offers
 - Preferred equity
- **History and Evolution of GP-led secondary transactions**
 - Historically used by “zombie” funds and lingering assets that were difficult to liquidate
 - Today, GP-led secondaries are a common way to provide LPs with the option of early liquidity while allowing other LPs the opportunity to continue to remain invested in the asset(s).
 - Often used with long-life “trophy” assets and cash flow generating investments.
 - Can be used as a way to seed new funds or strategies and appeals to long-term buyers.
 - Permits sponsor to retain control and economics while minimizing risk execution.

What are GP-Led Secondary Transactions?

- GP-organized process to proactively offer liquidity to existing LPs and to secure additional time and/or capital for a fund's unrealized investments
 - LPs are often given the option of (1) preserving their *status quo*, (2) receiving early liquidity, or (3) rolling into a new "continuation fund" (buyer) which may be paired with the option to increase exposure.
- Drivers include:
 - Liquidity demands from LPs
 - Desire from secondaries buyers for access to mature PE assets
 - Capital needs of existing portfolio companies (defensive and offensive)
 - Timing mismatch between fund life and asset management/exit plan
 - Market events
- Structures and terms are highly bespoke – no two deals are the same
 - Can involve a single asset or a portfolio of multiple assets (including the entire fund or a "strip sale")
 - Buyer usually provides additional "primary capital" to fund follow-on investments
- Buyers are typically secondaries funds or sophisticated institutional investors
 - Secondaries fund sponsors are increasingly raising dedicated funds to invest in GP-led deals
 - Often will "lead" the investment into the continuation fund (and negotiate terms vs. sponsor)

Transaction Objectives for GP-Led Secondaries



THE GENERAL PARTNER

Franchise Objectives

- ✓ **Introduce new investors to platform** with primary capital capabilities and **potential to support future fundraises**
- ✓ **Raise follow-on capital** to fund organic growth and execute on acquisition pipeline

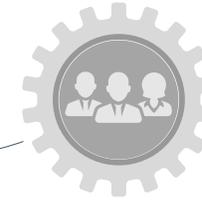
Economic Objectives

- ✓ **Secure new fees and carried interest terms** with new LPs and existing co-investors as applicable
- ✓ **Consolidate co-investors** into a uniform fee paying investment structure, **creating meaningful alignment going forward**
- ✓ **Monetize and de-risk accrued carry** through an accelerated realization event
- ✓ **Extend ownership and provide additional runway** to execute on value creation strategy



EXISTING LPS & CO-INVESTORS

- ✓ **Price maximization** achieved through **robust, arm's-length auction process**
- ✓ Provides a **non-coercive liquidity option** to existing investors
- ✓ Ability for existing investors to **crystallize attractive returns** in abbreviated hold period
- ✓ **Option to participate in the next phase of growth** through participation in the new vehicle
- ✓ New incentive package **re-aligns go-forward investment team**

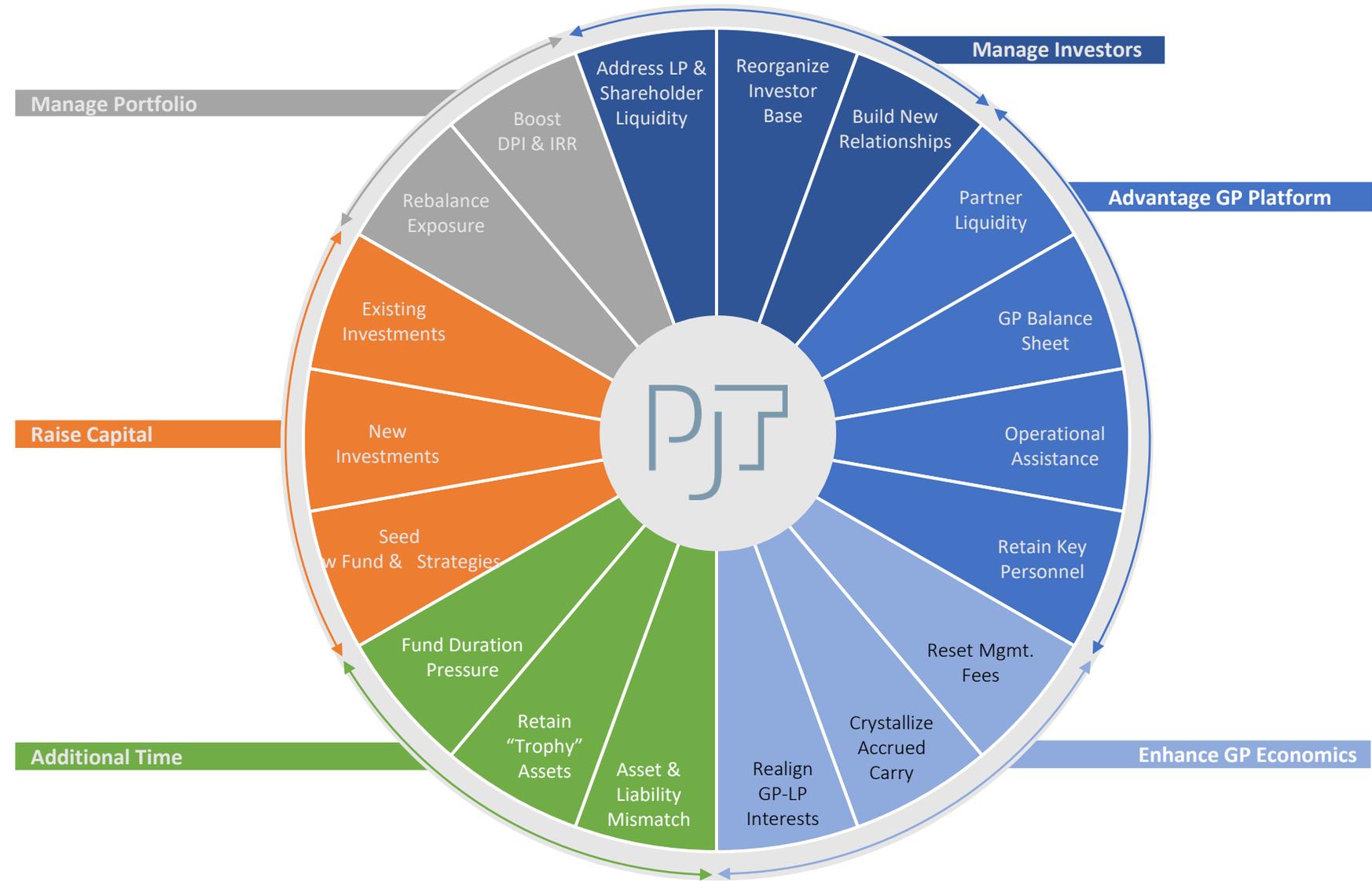


NEW LIMITED PARTNERS

- ✓ **Continuation Fund accentuates GP alignment** relative to other investment structures (e.g., LP interests, co-investment)
- ✓ Provides **exposure to trophy asset(s) in scale and concentration** inaccessible in traditional LP secondary markets
- ✓ Opportunity to **expand existing GP relationships** and partner with a seasoned sponsor with **differentiated sector expertise**

Transaction Drivers Are Increasingly Becoming Multi-Faceted

Sponsors are leveraging the secondary market to benefit their platforms by solving for an ever-growing number of strategic objectives



Evolution of the GP-Led Secondaries Market

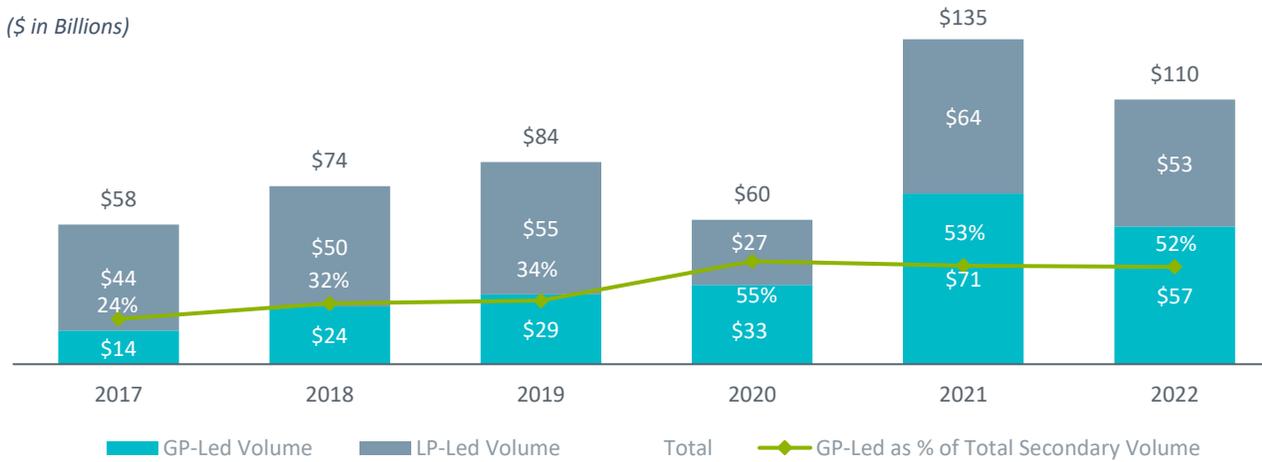
- Historical perspective on GP-Led Secondary Transactions
 - Almost all secondary transactions were traditional LP interest sales
 - GP-led transactions suffered from “zombie fund” stigma
- Recent years
 - GP-led transactions are increasingly viewed as a smart portfolio management tool
 - Leading sponsors in Europe and the U.S. are now able to access this market without it being viewed as a sign of weakness
 - Growth in GP-led transaction volume and techniques is expected to continue

Evolution of Key Secondary Market Statistics

FY 2022 GP-led transaction volume was \$57BN despite a volatile macro-economic environment impacting underlying portfolio company performance and valuation over the course of the year

SECONDARY MARKET TRANSACTION VOLUME

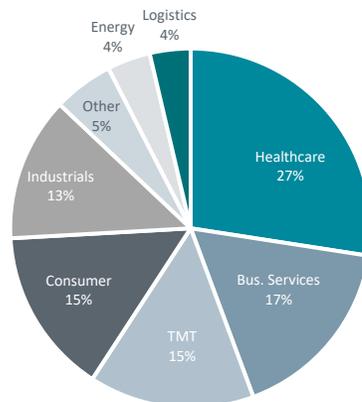
(\$ in Billions)



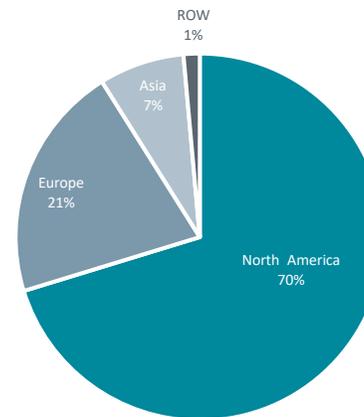
PJT INSIGHTS

- > Despite significant headwinds, GP-led market volumes in 2022 were the 2nd highest on record
- > Diversified industry distribution as investors navigated volatility across all sectors
- > Healthy GP-led transaction volume in Europe and Asia provides a framework for additional growth in 2023
- > We are optimistic that the current momentum will continue despite fundraising constraints, deployment pacing and valuation uncertainties
- > Currently, PJT is tracking over \$180BN of deal activity in the marketplace

GP-LED VOLUME BY ASSET CLASS

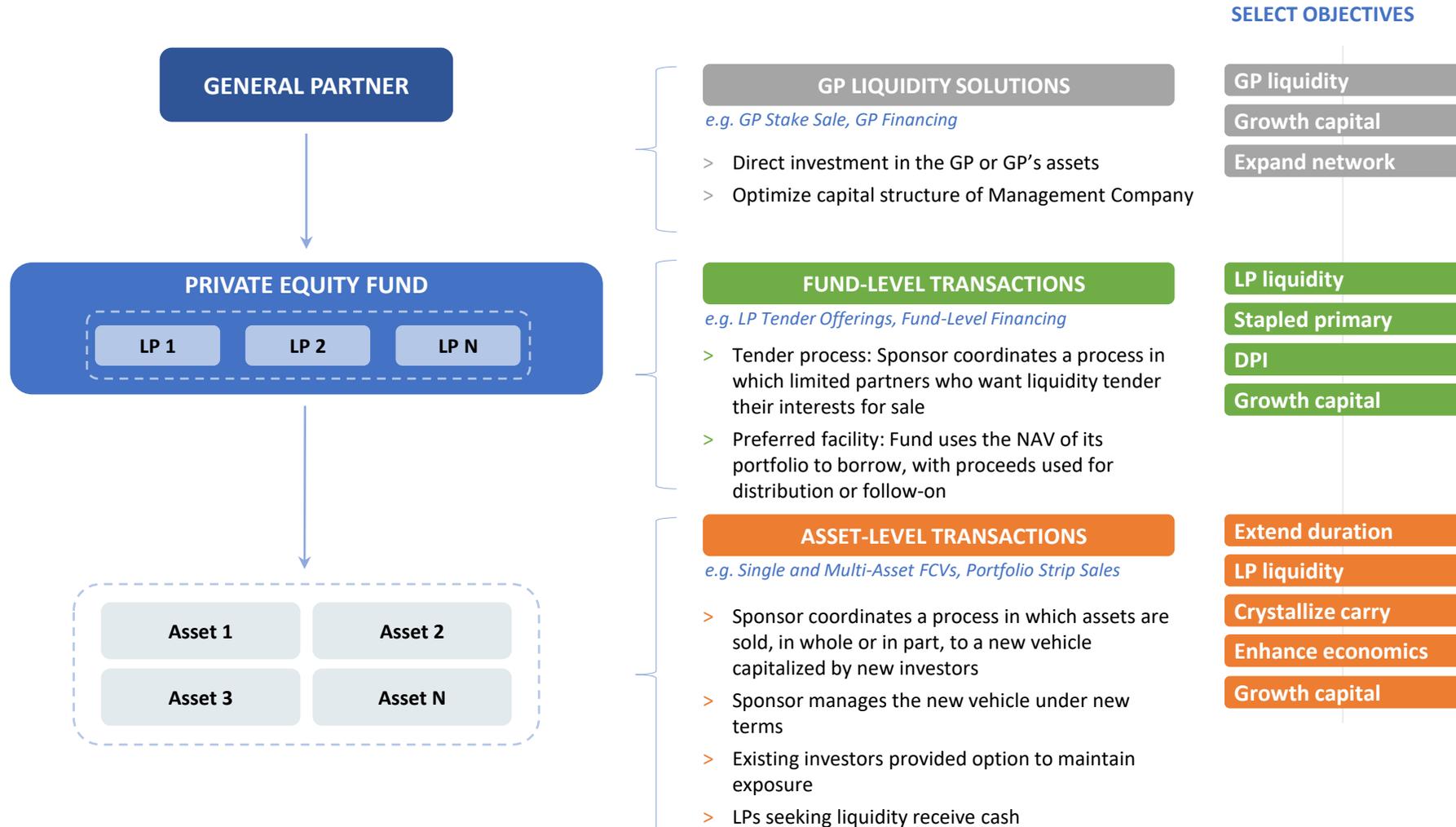


GP-LED VOLUME BY REGION



Overview of GP-Led Capital Solutions

The secondary market provides innovative transaction alternatives to traditional corporate finance solutions at the asset, fund and management company level



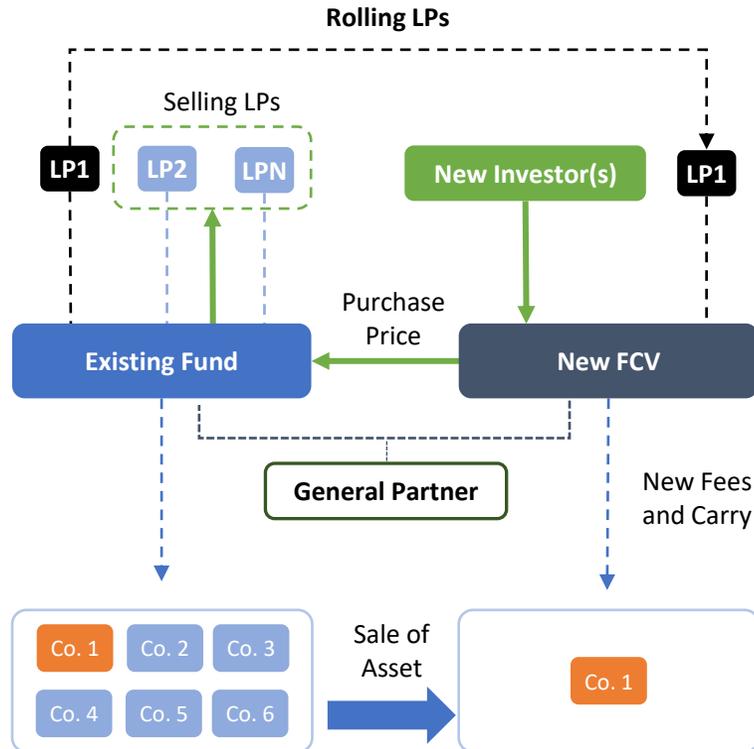
Types of GP-Led Secondary Transactions

Asset-Level			Fund-Level		Management-Company Level	
Single-Asset FCV	Multi-Asset FCV	Portfolio Strip Sale	LP Tender Offering	Fund-Level Financing	Equity Stake Sale	GP Financing
Transaction Description						
> Sale of an asset to a new FCV capitalized by new and existing investors and managed by the current sponsor	> Sale of all or a subset of the remaining assets of a fund or funds to a new FCV capitalized by new and existing investors and managed by the current sponsor	> Sale of a portion of the remaining assets of a fund or multiple funds to a new FCV capitalized by new and existing investors and managed by the current sponsor	> Limited partners are offered a liquidity option for their interest in a fund or multiple funds	> Capital is raised via a new senior security that is collateralized by the cash flows of all or a subset of the remaining assets in a fund	> Sale of a minority interest in the management company of a sponsor	> Capital is raised via a new senior security that is collateralized by a sponsor's economic participation in a fund or group of funds
Transaction Applicability						
> Extend hold period for strong performing "trophy" asset	> Select assets requiring more time and/or capital to maximize value	> Re-balance portfolio and reduce over-exposure to certain assets	> Optimize investor base through an organized liquidity event	> Flexible capital that can be used for follow-on or de novo investments	> Secure capital to address succession plans or seed new investment strategies	> Secure capital to fund GP commitment to new funds
Select Transaction Benefits						
<ul style="list-style-type: none"> ✓ LP liquidity ✓ Extend duration ✓ Growth equity ✓ Crystallize GP economics 	<ul style="list-style-type: none"> ✓ Full/partial LP liquidity ✓ Extend duration ✓ New equity ✓ Crystallize GP economics 	<ul style="list-style-type: none"> ✓ Partial LP liquidity ✓ Ability to recycle proceeds ✓ Crystallize GP economics 	<ul style="list-style-type: none"> ✓ Full LP liquidity ✓ Raise stapled capital ✓ Non-invasive ✓ Limited GP involvement 	<ul style="list-style-type: none"> ✓ Quick and efficient process ✓ Upside value retention ✓ No recourse on assets 	<ul style="list-style-type: none"> ✓ GP liquidity ✓ Raise growth capital ✓ Expand investor network 	<ul style="list-style-type: none"> ✓ Raise growth capital ✓ Expand investor network

PJT has advised financial sponsors across these transaction alternatives

Transaction Overview: Single-Asset FCV

ILLUSTRATIVE TRANSACTION STRUCTURE



DESCRIPTION

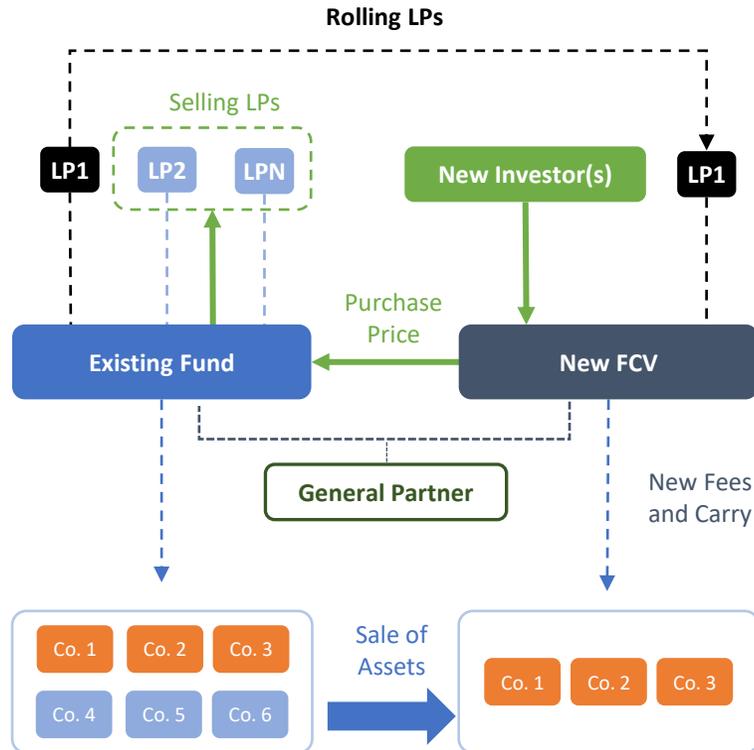
- > Sponsor sells all or a portion of a portfolio company to a new FCV
- > New FCV is capitalized with new investors and rolling LPs
- > Transaction proceeds are distributed to fund LPs
- > Sponsor continues management of the new FCV

SELECT BENEFITS

- > **Optional liquidity event** for LPs
- > **Extends duration** to maximize the company's value creation potential
- > Potential to secure new capital for follow-on investment(s) and/or debt refinancing
- > Ability to reset sponsor economics
- > Transaction price provides a true sale valuation
- > Usually does not trigger change of control provisions

Transaction Overview: Multi-Asset FCV

ILLUSTRATIVE TRANSACTION STRUCTURE



DESCRIPTION

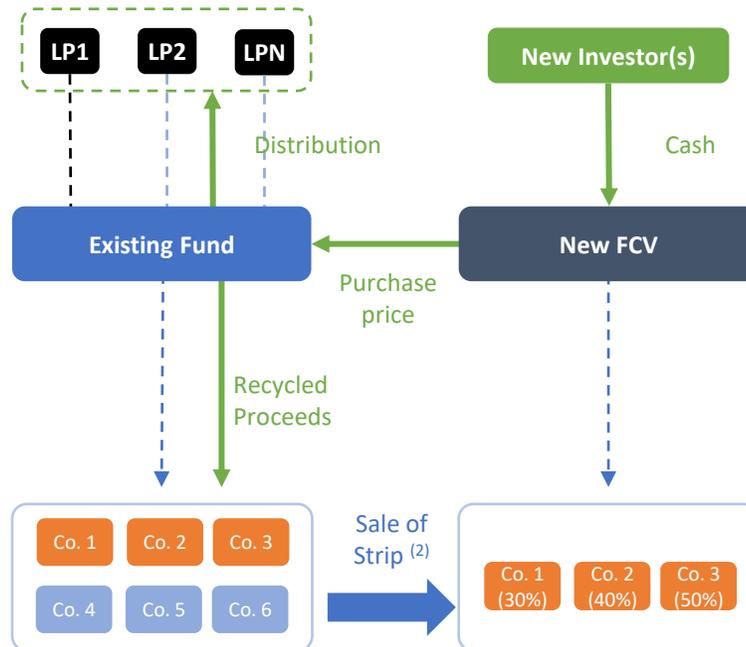
- > Sponsor sells all or a subset of assets across a fund or multiple funds to a new FCV
- > New FCV is capitalized with new investors and rolling LPs
- > Transaction proceeds are distributed to fund LPs
- > Sponsor continues management of the new FCV

SELECT BENEFITS

- > **Optional full or partial liquidity event** for LPs
- > **Extends duration** to maximize the company's value creation potential
- > Potential to secure new capital for follow-on investment(s) and/or debt refinancing
- > Ability to reset sponsor economics
- > Transaction price provides a true sale valuation
- > Usually does not trigger change of control provisions

Transaction Overview: Portfolio Strip Sale

ILLUSTRATIVE TRANSACTION STRUCTURE



DESCRIPTION

- > Sponsor sells an equity “strip” in all or a subset of portfolio companies across a fund or multiple funds to a new FCV
- > Transaction proceeds are distributed to fund limited partners or recycled back into the fund(s)
- > Sponsor typically continues management of the new FCV

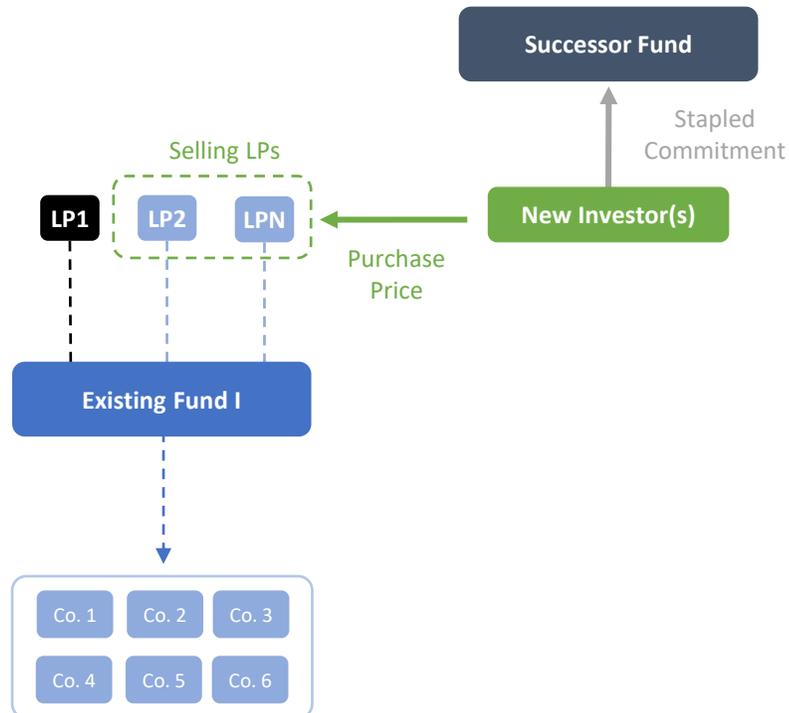
SELECT BENEFITS

- > Provides partial liquidity to limited partners
- > Re-balances portfolio **company exposure**
- > Proceeds can be recycled to invest in new deals or follow-on investments⁽¹⁾
- > Limited to no change in fund duration or governance for younger funds
- > Attractive for resilient portfolios with limited valuation adjustments

1) Subject to LPA amendment / LPAC approval.
 2) Denotes illustrative equity sale percentage.

Transaction Overview: LP Tender Offer

ILLUSTRATIVE TRANSACTION STRUCTURE



DESCRIPTION

- > Limited partners are offered a liquidity option for their LP interests in a fund or multiple funds
- > Price discovery process is established through a true arm's length auction process
- > Transaction does not affect the existing fund waterfall

SELECT BENEFITS

- > **Non-coercive liquidity event for LPs**
- > **Expedited transaction timeline** relative to other GP-led transactions
- > Transaction typically **yields higher price for selling LPs** than a traditional LP secondary sale
- > Potential for sponsor to secure **stapled primary commitments**
- > Ability to **target select investors and optimize limited partner relationships**
- > The transaction **typically does not require LPAC consent**

Regulatory Updates & SEC Scrutiny

- SEC Proposed Rules (Release No. 5955; February 9, 2022) would *require fairness opinions* for GP-led secondaries, which would be required to be shown to all investors.
 - SEC Proposal defines GP-led secondaries as a transaction initiated by the GP or an adviser and would include a transfer or sale to a Continuation Fund.
 - Fairness opinions are common, but mandating them in all cases would be an expansion of federal securities laws and increase cost burdens on investors.
 - Fairness opinions not necessarily responsive when “price” and consideration are not solely cash.
 - Other mechanisms for price discovery (competitive sale process, third-party valuation, etc).
- Beyond the New Proposed Rules, SEC staff have expressed concerns about various aspects of GP-led transactions
 - The co-head of OCIE’s Private Funds Unit has expressed concern that a sponsor’s competing duties and interests on the buy-side and sell-side, coupled with its control over the information provided to investors, creates a situation that is “ripe for misinformation and offering fraud”
 - Failures to provide adequate disclosure about the sponsor’s valuation determination and process, existing LPs’ options and the sponsor’s conflicts of interest (including in connection with “stapled secondary” transactions, where an incoming secondary investor also commits to make a primary investment to the sponsor’s future fund)
 - Failures to identify principal and agency cross transactions and to comply with related regulatory or compliance requirements or to comply with notice and consent requirements under fund documents
- The SEC has brought enforcement actions against sponsors (and in certain cases, their founders) relating to GP-led secondary processes

Other Regulatory Updates and ILPA Scrutiny

- **Europe**

- Currently no clear regulatory guidance from European regulators
- French regulatory authorities have expressed concerns about conflicts of interest in secondary transactions
- Consider application of AIFMD to a continuation fund vehicle

- **ILPA (Institutional Limited Partners Association)**

- ILPA, the LP trade group, issued guidance on best practices in GP-led secondary fund restructurings
 - Importance of LP engagement and disclosure regarding rationale for transaction, involvement of financial advisors and conflicts of interest
 - LPs should have access to portfolio company diligence materials provided to secondary buyers
 - LPs should be given sufficient time to make elections (not less than 20 business days)
 - Default option should be “status quo”
 - Transaction fees and expenses should be disclosed and allocated according to existing fund documents and/or based on which parties benefit from the transaction

Conflicts of Interest & Fiduciary Duties

- The related-party nature of GP-led cross-fund transactions means that a number of conflicts of interest and fiduciary duty issues inherently exist:
 - Fairness of valuation determinations
 - Recent SEC proposal to require fairness opinions in GP-led secondary transactions
 - Other mechanisms for price and value verification
 - Fairness of the transaction process to existing limited partners/LPAC (and, in the case of fund-to-fund transaction, to the limited partners/LPAC of the buying fund)
 - Adequacy of disclosures
- Given that the sponsor serves as a fiduciary on both sides of the transaction, the goal is to structure the transaction in a way that successfully mitigates the various conflicts of interest
 - Fund documents may require LPAC consent for the sale from Selling Fund to the Continuation Fund
- If the sponsor and/or its controlling persons, in the aggregate, own more than 25% of any fund entity participating in a GP-led cross-fund transaction, the transaction would also be a principal transaction subject to the consent requirements of Section 206(3) of the Advisers Act

Conflicts of Interest & Valuations

- Price discovery is key
 - GP often retains an investment bank to run an auction process
 - Typically at the outset of the transaction
 - Less commonly, post-signing pursuant to a go-shop provision
 - Fairness opinions
 - In many cases, it may be appropriate to engage separate financial advisors to opine on the fairness of the valuation from the selling fund's and the buying fund's perspective, respectively
 - Fairness opinions are common and may become moreso after SEC proposed rules
 - An unconflicted third-party seller (or, in a fund-to-fund transaction, an unconflicted third-party buyer) can help validate the pricing by participating in the transaction based on the same valuation
 - GP may seek LP or LPAC approval of its valuation determination
 - May need to reconsider pricing if asset valuations materially change during election period
- GP should provide investors with detailed disclosure about its valuation determination and process

Conflicts of Interest & Consent Solicitation

Process

- Provide fair options to investors
 - Allow the LPs to maintain the “status quo” in their investment
 - Status quo should be the default result for any LPs that do not respond
- Avoid any coercive element
 - LPs should be asked to separately elect whether to (i) consent to the transaction and (ii) cash-out or roll-over to the continuation fund
 - If any special terms are offered to certain (but not all) LPs, or to new investors only, consider whether such special terms should be disclosed in the consent solicitation materials (*i.e.*, so that the sponsor is not subsequently viewed as having bought consent)
- LP (or LPAC) approval of the transaction and waiver of any conflicts may be required (or otherwise advisable)
- Give LPs/LPAC sufficient time to make an informed decision
 - Sponsors typically provide at least 20 business days, consistent with the SEC tender offer rules
 - ILPA recommends a minimum of 30 calendar days

Best Practices in Building LP & LPAC Support

Investor communication and process management is paramount to a successful transaction

LP Focus: Consistent Communication

- Consistent communication during the transaction process is central to a successful transaction
- Key LPs should be engaged early in the process to control process messaging and to ensure their awareness of major transaction milestones

LPAC Focus: Ensuring a Fair, Arm's-Length Process

- Existing investors will need to receive comfort that an arm's-length price discovery process was run and that the transaction was completed at fair levels
- The motivation for pursuing the transaction, options for the existing investors and detail on alternative routes explored need to be clearly set out

Key LP Communication Milestones

Timing	Message
1 Initial Outreach	> Brief description of process / structure being contemplated and key rationale for pursuing
2 Intermediate Check-In	> Informal one-on-one updates with key LPs to update them on the transaction and any material changes from previous conversations
3 Election Period	> Explanation of the process, the options available, the mechanics and impact to their existing capital account

Key Components of a Successful Transaction

- > **Disclosure**
 - The sponsor should **engage the LPAC early in the process** and provide **regular updates** on process, pricing and structure
 - LPs should be afforded **sufficient time to review** the proposed transaction and make elections
 - LPs should have **access to data room materials** provided to potential buyers
- > **Arm's-Length Process**
 - **Financial advisors** should be engaged by the sponsor to conduct a rigorous, arm's-length process
 - **Fairness opinion** can be utilized to support the transaction price

Fairness to Investors

- Rolling LPs should participate in the new vehicle on terms that are substantially similar to (or otherwise no less favorable than) the existing fund's terms
 - This may mean having separate classes of interests in the new vehicle
 - It may be appropriate for rolling LPs to go into a different vehicle than the secondary buyer
- Rolling LPs will want the transaction structured tax-free
 - May be effected as an in-kind distribution and subsequent re-contribution to new vehicle
 - Additional structuring may be necessary for certain investments (e.g., flow-through deals) and certain investors (e.g., non-US, sovereign wealth funds)
 - Be mindful of investors' tax sensitivities and any tax covenants given to rolling LPs under the existing fund's governing documents or side letters
- Buy-side representation
 - Buy-side investors will want to be sure that the transaction is fair from the buying fund's perspective
 - Clients will sometimes retain two law firms to provide a more arm's-length negotiation of the deal documents
- GP's carried interest
 - Selling LPs: GP's carry is crystalized with respect to selling LPs as of transaction reference date
 - Rolling LPs: GP's carry is typically rolled into the new vehicle with respect to rolling LPs

Investor Disclosure & Transparency

- Sponsors should provide specific and particularized disclosure to existing and potential investors in connection with the investor/LPAC consent solicitation process
 - Description of the proposed transaction
 - The sponsor's rationale for the transaction (including the decision to engage in the transaction with a related party instead of a third party buyer)
 - Detailed information about portfolio companies
 - Information about sponsor's financial model and expectations regarding the future of the portfolio
 - Information about the process and methodologies used by the sponsor to establish (and verify the fairness of) its valuation determination
 - Comprehensive risk factors and conflicts disclosure
 - Clear and detailed disclosure regarding the allocation of transaction-related fees and expenses
 - In particular, GP should specify who pays broken deal expenses if the transaction is not consummated
 - Other material information that may be necessary in order for the LPs/LPAC to make an informed consent and election decisions in connection with the transaction
- Where possible, existing LPs and new investors should have access to the same diligence materials regarding the transaction and the underlying assets

Terms of the Continuation Vehicle

The economic and governance terms of the new vehicle are negotiated by the secondary buyer and rolling LPs

- **Distribution waterfall**

- The new fund's waterfall may be more complex than a traditional private equity waterfall, including multiple tiers of performance hurdles before the GP receives carry
- Rolling LPs may be offered a menu of waterfall options to select from (in addition to "status quo" option)

- **Additional capital**

- The amount of uncalled capital available from new and rollover investors, recycling provisions, and limits on the new fund's ability to make follow-on investments, are frequently negotiated points
 - GP should carefully consider the portfolio and its anticipated funding needs

- **Governance**

- The secondary buyer(s) will often negotiate favorable GP removal rights, fund and portfolio company board representation and other control and transparency rights

- **GP alignment**

- The GP will often be required to increase its commitment to the new fund vehicle to promote alignment with investors

Transactional Issues in GP-Led Secondaries

- Many of the same transactional issues that arise in third-party sales are present in GP-led transactions
 - Regulatory issues, tax structuring, debt financing, third-party consents, etc.
 - M&A attorneys need to be involved from the beginning
- Allocation of transaction liability / indemnification responsibility
 - Secondary buyers often want reps about the business but the selling fund/LPs are typically not willing to accept liability
 - Another reason why transactions typically priced at a discount to NAV
 - Can be addressed through the purchase of rep and warranty insurance
 - GP will occasionally accept responsibility for certain liabilities (i.e., no challenge to the transaction, accuracy of information provided, etc.)
- Consents to transfers from lenders and other third parties
 - Indirect ownership changes may trigger consent requirements even if the assets stay under common control
- Tag-alongs, rights of first refusal and other rights may be applicable at the portfolio company level
 - Applicability will often depend on “affiliate transfer” provisions in company documentation and how fund restructuring is structured
- Short-swing trading reporting obligations and liability risk under Section 16 of the 1934 Act
- MNPI disclosed to LPs and LPAC members may impose trading restrictions on LPs and their representatives and could, in certain cases, require a portfolio company to accelerate public disclosures about the potential transaction