

## New York State Comptroller Bans Placement Agents, Paid Intermediaries and Lobbyists in Investments with the Common Retirement Fund

On April 22, 2009, New York State Comptroller Thomas DiNapoli imposed a ban on the use of placement agents, paid intermediaries and registered lobbyists with respect to the state's \$122 billion Common Retirement Fund (CRF), including arrangements under which any of these persons are compensated on a flat fee, contingent fee or any other basis. New York City Comptroller William C. Thompson, Jr., is calling for a similar ban to be adopted by the trustees of the New York City pension funds, which hold \$82.5 billion in assets.

Soon after Comptroller DiNapoli announced this ban, he released the "New York State Common Retirement Fund Placement Agent Disclosure Policies and Procedures of the Office of the State Comptroller" (the "Policy") formalizing the ban on the involvement of placement agents, paid intermediaries and registered lobbyists in investments with CRF.<sup>1</sup> Comptroller DiNapoli has called on the New York Insurance Superintendent, Eric Dinallo to codify this ban in CRF regulations. In addition, Comptroller DiNapoli plans to submit proposed legislation to the New York State Assembly to codify his reforms and to enact additional pension system reforms in New York. This ban will have a significant effect on investment advisers, managers and consultants dealing with CRF.

The Policy issued by Comptroller DiNapoli, dated April 21, 2009, sets forth the Comptroller's general policy reasons for banning the use of placement agents, registered lobbyists and other intermediaries (collectively defined as "Placement Agents") and

describes the mandatory disclosure requirement under which outside investment managers (Investment Managers) working with CRF must represent in a letter prior to completion of any investment transaction that the Investment Manager has complied with the Comptroller's ban.

The following is a summary of the Policy.

### Comptroller's Policy Statement Regarding Use of Placement Agents by Investment Managers (Policy, p. 1)

- The Comptroller has determined that it is in the best interest of CRF to prohibit CRF from directly or indirectly engaging, hiring, investing with or committing to an Investment Manager that is using the services of a Placement Agent for assistance in obtaining investments by CRF or otherwise doing business with CRF regardless of whether compensated on a flat fee, a contingent fee or any other basis.
- The disclosure and notification requirements described in the Policy are mandatory for all Investment Managers doing business with CRF.
- The stated goals of the Policy are to prevent actual and apparent conflicts of interest in CRF's investment decision-making process, to ensure the integrity of the decision-making process and to ensure that all decisions are made to benefit CRF's participants and beneficiaries.
- Moreover, it is the stated policy of the Comptroller that CRF investment staff will not use Placement

Agents as part of the investment decision-making process, and that the use of Placement Agents is unnecessary because all potential Investment Managers have open access to CRF investment staff.

### Certain Investment Managers Must Provide CRF with a “Placement Agent Disclosure Letter” Representing Compliance with the Comptroller’s Ban on Placement Agents (Policy, §§ I, II and III, and Exhs. A and B)

- Any Investment Manager that either has a direct contractual investment-management relationship with CRF or with an investment vehicle in which CRF is invested (Direct Investment Managers) or has an indirect contractual investment management relationship with CRF through an investment vehicle that invests in funds or other pooled investment vehicles or other assets and for which CRF can decline recommended investments or otherwise exercise discretion (Indirect Investment Managers), must provide a Placement Agent Disclosure Letter (Letter) addressed to all CRF’s consultants and advisers (initially listed in Exhibit B to the Policy).
- The Policy provides specific requirements for Letters with respect to private equity investments (Exhibit A-1) and public equity managers (Exhibit A-2). Requirements with respect to the substance of each Letter are the same, but Exhibit A sets forth certain mechanical distinctions relevant to the different transactions contemplated.
- Each Letter must represent: (i) that the Investment Manager did not use a Placement Agent; (ii) that no benefit has been paid, given or promised to any of CRF’s consultants or advisers (including any affiliates and any person reasonably believed to be an officer, director or employee of such consultant, adviser or affiliate, or of CRF or of the Comptroller’s Office) in relation to obtaining (a) an introduction to the CRF or any officer or employee of the Comptroller, (b) other assistance in obtaining business from CRF, or (c) a favorable recommendation with respect to the covered investment transaction; and (iii) that all information contained in the Letter is true, correct

and complete in all material respects. CRF may publicly disclose all information in such Letters.

- Fees paid by a General Partner to its legal counsel and accountants in connection with the organization of the Partnership and the offering of limited partner interests therein are exempted from the Letter requirements so long as its legal counsel and accountants have not also represented CRF in connection with its investment in the Partnership or been involved in any form of solicitation relating to CRF.

### Failure to Comply with Placement Agent Disclosure Letter Requirement May Result in Termination of the Investment Relationship (Policy, §§ III and IV, and Exh. A)

- The Policy provides that the sufficiency of disclosure by an Investment Manager will be jointly determined by the Chief Investment Officer, the Inspector General and the Special Counsel for Ethics in the Comptroller’s Office.
- If an Investment Manager fails to comply with the Letter requirement, or if CRF determines that a Letter contains a material inaccuracy or omission, CRF shall have the option, in its sole discretion and without any liability, to terminate its investment relationship with the Investment Manager.
- The Policy gives CRF the sole right to determine whether a misstatement or omission is material and requires that any management agreement between CRF and an Investment Manager permit such termination by CRF without penalty.

### The Policy Sets Forth Certain Notice and Submission Requirements Relating to the Placement Agent Disclosure Letter (Policy, §§ V and VI, and Exhs. A and B)

- At the outset of a due diligence review for potential investment transactions, CRF must inform Direct Investment Managers, and Indirect Investment Managers must inform any underlying fund, in writing of the Placement Agent Disclosure requirements. Additionally, CRF or an Indirect Investment Manager, as appropriate, must provide written notice requesting a Letter.

- Within 20 calendar days from receipt of such notice, but no later than 15 calendar days prior to the closing of an investment transaction, the Investment Manager must submit the appropriate Letter to CRF, which will be provided to certain officials initially identified in Exhibit B to the Policy. As part of closing, an Investment Manager must also restate the Letter and confirm compliance.

## Endnote

<sup>1</sup> Available at <http://www.osc.state.ny.us/pension/place-mentagntdiscl.pdf>.

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*For more information about these policies and procedures, or any other matter raised in this Client Update, please contact one of the authors, listed below.*

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