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Bridgewater, Pershing Tiptoe on JOBS Act Sales Exemption

By Tom Stabile December 23, 2015

Some of the market's largest hedge fund managers have taken the plunge to seek federal exemptions allowing them to market their strategies publicly, including Bridgewater Associates, Pershing Square Capital Management, Lighthouse Partners, and Silver Creek Capital Management.

Yet none of them – and scores of their peers registering under the 506(c) general solicitation exemption added to the 1933 Securities Act's Regulation D in 2013 by the JOBS Act – are actively deploying these new tools to discuss their strategies publicly, publish performance results, or turn their websites into fundraising engines. Indeed, none of the big firms would comment publicly on why they had even sought the 506(c) exemption in lieu of the far more common 506(b) private funds rule that bars nearly all forms of general solicitation.

While early buzz that the JOBS Act would lead hedge funds to put up billboards and run TV ads for their products has fizzled, the more surprising development has been the willingness of funds large and small to seek the exemption but not actually employ it, says **Ted Eichenlaub**, partner at ACA Compliance Group.

"That's very consistent with what we're seeing in marketplace," he says. "We have very few clients – we can probably count them on one hand – that are taking advantage of 506(c). People like the perceived flexibility of it, but firms are more hesitant to use it."

The most hedge funds may be doing under the exemption is speaking more freely – or at least with less apprehension – when meeting potential investors at industry conferences, says **James Jalil**, partner and attorney at **Thompson Hine**. "People are still getting comfortable with it," he says.

However, that reluctance will disappear once the first big shop takes solid steps to use the general solicitation regime – and then the floodgates will open, says **Peter del Rio**, managing member of **Unicorn Capital Partners**, a new fund charging ahead with 506(c) marketing and sales capabilities.

"The genie is out of the bottle, and in five years, most of the alternative funds in the market are going to be 506(c) rather than 506(b)," del Rio says. "Once investors see the transparency [of returns], it will be a tectonic shift."

The first big firm to successfully use the general solicitation approach will see followers "popping up all over the place", he adds.

That scenario of how the general solicitation approach could gain momentum is certainly plausible, given the "herd mentality" among many alternative investment firms, Jalil says. It may not necessary overtake the existing private funds regime, especially if the biggest firms continue to have a fundraising edge, he says.

"But I tend to agree it will become more popular than it is now," he adds. "For now, they're letting somebody else blaze the trail."

An important factor that could encourage even more use is hedge funds realizing that the main burden of 506(c) rules – the need to verify the accreditation status of investors before accepting their capital – will actually be much less for managers that rely on institutional investors, Eichenlaub says.

"Whether it's three years or five years or ten years, it will start to happen when that one big firm does it," he says.

It's not clear if it might be one of the firms that has already taken the first step.

Bridgewater last year filed for the general solicitation exemption for its newly launched Optimal Portfolio, the first new strategy the $154 billion firm had launched in 20 years. It has raised $15.2 billion for the fund, and appears to primarily be targeting its existing institutional clients for mandates.

Bridgewater only filed for the 506(c) exemption from a "risk mitigation perspective", expecting that the new strategy would get a lot of media attention, says a source familiar with the firm's thinking who requested anonymity. Its site, however, has no prominent mention of the new fund.

The same goes for Pershing Square, which runs $22.3 billion and has $5.7 billion in a fund registered with a 506(c) exemption, according to an SEC filing from last month, as well as the $8.5 billion Lighthouse's SRI Global Long/Short Fund and the $7 billion Silver Creek's Opportunities IV Fund A offering.

Many other hedge funds that have filed for the exemption are not promoting their products, leaving it to Del Rio's firm and other small players to lead the charge.

Unicorn Capital has already filed for a 506(c) exemption for its Unicorn Macro Fund, and will file similarly for a new Unicorn Pairs Fund, which the firm is launching next month and is marketing on its website by offering a 5% minimum return for one year on $100,000 in seed capital. The website says a "proof of concept" version of the Pairs fund, which is targeting fund of funds managers and individual investors, has generated 20% annualized returns net of fees for more than two years.

Barac Capital Management also is using a 506(c) exemption to post performance data online for its Barac Value hedge fund, says **Ted Barac**, managing member of the small Florida-based shop. The $2 million fund has yet to seek investors beyond friends and family, but aims to get the word out in advance of future fundraising, he says.

"We're interested in building a track record and exposure for the fund," he says. "It allows us to publish quarterly letters, performance data, and have a website without protected passwords."

Many of the 506(c) exemption requirements may be daunting for hedge funds used to the current regime, Eichenlaub says. Firms especially are leery of having to submit their marketing materials to the SEC prior to publishing them, he says.

And most hedge funds, wealth management firms, and institutional investors all have invested considerably in their operations to work within the 506(b) world, he says.

"There's an established playbook for how to get to accredited investors without general solicitation," Eichenlaub says.

It also doesn't hurt that many larger hedge funds are not starving for capital right now. "If investors are lining up, they may feel they don't need 506(c)," he adds.

But those walls may break down once investors get a taste of the data they can get on hedge funds that do use the 506(c) rules to full effect, del Rio says.

"No one wants to stick their neck out because there's no competitive advantage yet," he says. "But when it happens, there's going to be a rush to the door."