Private Placement Assets: Hidden Time Bombs or Buried Treasure?

This article is intended for use by financial portfolio managers, trust administrators, attorneys representing trust and estate clients, persons who own or are interested in owning Private Placement investments, and business valuation practitioners who are interested in the real-world application of their art. This article is not intended to be theoretic and overly technocratic, since it is based directly upon professional experience, not mathematical formulas or theoretic studies. The author is not a licensed attorney in any jurisdiction, and this article should not be construed as legal advice or the practice of law under any circumstances.

In the world of professional wealth management, most persons prefer not to deal with the issues surrounding their clients' "Private Placement" assets: financial assets and tangible properties, which have little or no marketability. Such assets are difficult to price for portfolio administration purposes and sometimes evoke emotional attachments from clients, which interfere with rational decision processes. Most wealth managers prefer not to accept these asset classes in order to avoid difficulties. However, portfolio managers in the fiduciary world may have no choice in the matter. Executors / personal representatives of decedent estates may find themselves responsible for these assets after accepting appointment, sometimes unexpectedly, since these assets are not always disclosed beforehand. In some cases, a family may not even be aware of the existence of certain financial assets or real property owned by the decedent, until they are discovered by a thorough vetting. A trustee may unexpectedly become responsible for private placement assets after a revocable trust becomes irrevocable, or a person who had formerly served as an investment advisor for the asset in question is no longer able to act.

Despite wealth managers' aversion to these asset classes, they are frequently accepted into fiduciary relationships anyway. Private Placement assets can be difficult to legally separate from a client's wealth pool, and commissioned new business personnel at wealth management institutions will try to overlook the existence of problematic situations in order to bring in new accounts. Moreover, financial institutions frequently inherit difficult fiduciary accounts from corporate acquisitions. Thus, most fiduciary wealth managers are generally challenged with the task of managing Private Placement assets at some time or another. Many fiduciary wealth managers are simply unaware of the existence of these assets in their portfolios, because they are simply not looking for them. Bank trust departments which do recognize these assets frequently refer to them as "Unique Assets", "Closely Held Assets", or "Special Assets".

Time Bombs?

The mere existence of Private Placements in a fiduciary portfolio presents a potential "Time Bomb" scenario, particularly if a trustee is unaware of the asset. There are established government regulations pertaining to the administration of Private Placement assets within fiduciary accounts. However, government regulators have traditionally been disinterested in addressing these asset classes, perhaps simply out of lack of understanding. A more potentially dangerous exposure exists from fiduciary breaches which can occur from neglect. Simply ignoring a potentially problematic asset is similar to ignoring a developing medical condition or an annoying squeaking noise from your car's brakes; inaction can magnify the eventual detrimental effects.

A good example would be the ownership of abandoned real property. How frequently has one had a client who owned an unimproved or remotely located real property somewhere, in which no one took an interest? Regardless of whether or not such a property is placed on record as a fiduciary asset, this asset is owned by a trust if it is registered as such on the books of a county assessor / recorder. Even if such property is still entitled in the name of a deceased person, it may still ultimately be a trust asset if all decedent estate assets were "poured over" by estate settlement, thus creating a liability exposure for a fiduciary. In the example scenario of an abandoned property, what will happen when a small child is injured on said property, illegal dumping occurs, or even an environmental infraction is discovered? If a fiduciary asset manager has been failing to deal with the administration of such a property, it is most likely not insured and no monitoring of the property has been enacted. Any tort lawsuit claims or governmental fines should be assessed directly to the negligent fiduciary. Valuable personal property can also present a problem if not detected by a fiduciary. What if a fiduciary client had a collection of valuable art items and they were not properly inventoried and maintained by the trustee?

A more extreme example of liability exposure for a fiduciary asset manager exists in the case of a family business. Those of us who are experienced in the wealth management industry are aware that a large segment of wealthy persons have obtained their wealth from the creation of a successful business enterprise. Successful entrepreneurs frequently become fiduciary clients and are also inclined to place portions of the equity in their business enterprises into trust accounts for the benefit of their relatives. Lawyers drafting trust documents frequently write some manner of exculpatory clauses pertaining to these types of financial assets into trust documents, so that corporate trustees will be more likely to accept the relationship. However, most of these clauses are not strongly worded and could easily be challenged in court by a disgruntled remainder beneficiary. Even in the case of the existence of exculpatory language, fiduciary asset managers need to be wary and should not abandon administrative obligations.

Suppose that Company A is a successful restaurant located in a tourism “hot spot”, which was excellently managed in the year 2015 by its founder and veteran restaurant operator, Mrs. A. Company A was a cash cow, which was distributing large amounts of cash to its equity owners, even after paying Mrs. A a generous salary. Mrs. A has transferred 20% non-controlling interests in Company A to her four family members, none of whom have taken an active interest in the business. Mrs. A has reserved the right to manage the affairs of Company A for herself, pursuant to the terms of Company A’s governing documents, and thus maintains complete control despite only owning 20% of its equity. Trustee X is the administrator of the four family trust accounts, and the 20% ownership interest in Company A constitutes a 75% asset concentration for each trust. Moreover, each of the four trust income beneficiaries is heavily dependent upon the income distribution from the restaurant for their personal expenses. Trustee X has accepted appointment as trustee because of longstanding commercial relationships with Company A and Mrs. A, and has obtained exculpatory language in the trusts’ governing documents allowing for retention of Company A as a portfolio asset.

This entire scenario is fraught with potential perils for a fiduciary, not because Company A is a bad portfolio asset, but rather because it is a good one! There is nowhere to go but down. Very real possibilities of asset valuation impairment exist here, which an experienced business person should recognize. First of all, the four trusts have a highly weighted asset concentration in Company A, and the old adage “Don’t put all your eggs in one basket” is always relevant in the investment community. Lawyers representing the fiduciary should very scrupulously scrutinize trust document language in such an instance.

Problems can arise for Company A from routine business administration issues. For instance, what if Mrs. A is really hiding some of the profits from the operation of Company A. Did the other equity interest holders (e.g. Trustee X) take any prior preventative action to prevent fraud, such as request an audit of the company books? Have financial statements been obtained by Trustee X and credibly examined? A more likely problem scenario is the loss of Mrs. A’s managerial services because of death or inaction. If Company A has absolutely no succession plan for such an event, the business will rapidly dissipate into nothing and the valuable cash cow owned by the four trusts will become worthless. Did Trustee X take any prior action to ensure a succession plan or exit strategy for Company A? A person with experience in the arena of Private Placement investing will most likely address such issues beforehand. Did Trustee X utilize such a person?

Other issues can arise merely because of the taxation consequences particular to the ownership of business interests in general. The income taxation events for Private Placement assets are generally more difficult to account for than those of the typical marketable securities portfolio. While tracking the cash dividend income from C corporations is not usually problematic, correctly booking cash distributions from S corporations and partnerships can be, because of the varying application to trust principal and income. Errors in the application of these cash receipts might not only violate the Internal Revenue Code but also state laws pertaining to trust principal and income distribution and expose the fiduciary to tort liability by remainder beneficiaries. Certain Private Placement assets, such as S corporations and partnerships, present difficulties in the area of tax cost basis determination also.

Estate and gift taxation issues might also be relevant, because of valuation issues. Federal government regulations require the valuation of Private Placement assets on an annual basis. If a decedent estate or trust is subject to estate taxation, these valuations might be considered relevant by an examining taxation authority. In the event that a fiduciary fails to account for a Private Placement asset on its books and subsequently fails to report said asset on an estate tax filing, the potential for a tax fraud implication exists. If a fiduciary has not maintained its trust records accurately and has failed to remove expired assets from its ledger, the potential for taxation overpayment exists. Inaccurate valuation can also lead to tax overpayment problems also.

A good example would be private equity or hedge fund interests, which are frequently popular with high net worth clients. Most fiduciaries simply report such financial interests on their books at their reported “Fair Value” as provided by the fund manager or its agent. Accounting rules governing fair value determination are governed by ASC [Accounting Standards Certification] Topic 820, which is, of course, subject to continuing revision, just as all accounting standards. Concisely, the recommended method for valuing fund portfolio interests are to segregate valuation determinations into three levels: Level 1: Quoted Prices; Level 2: Observable Inputs Other Than Quoted Prices; Level 3: Unobservable Inputs. In reality, the fair value determination frequently refers to the initial purchase price of a fund portfolio asset, a subsequent investment tranche financing for a portfolio asset, or a remote transaction in the fund’s interest by an exiting member. While this might sound logical at first, those of us with first hand experience in administering these funds know that such approaches are cursory at best. Few assets of any investment class are worth the same value as their purchase price from several years ago; the pricing of investment tranche investment prices usually has more to do with marketing efforts than investment analysis; and transactions prices from fund withdrawal (when allowed) may be performed under duress, since there is no liquid market for these interests. Moreover, a fund manager could manipulate the price of a portfolio company by transacting a minor stock purchase. If one tracks the investment performance of individual fund assets from fund inception until asset liquidation, it is generally discovered that the ultimate disposition value of a fund asset has little relation to its historically presented Fair Value.

So, does that mean that a fiduciary cannot rely on Fair Value for portfolio valuation reporting? In reality, there is little choice but to accept a fund manager's Fair Value, at least as a basis. Whereas a fund manager would have access to the books and records of its portfolio companies, a fund member will not. However, something which is rarely considered by fiduciary asset managers are the liquidity impairment implications of the private equity / hedge fund agreements. These agreements almost always severely restrict or even prohibit the sale of interests in their funds, thus severely impairment short-term value of the investment. If a fiduciary asset manager reports the value of a decedent client's private equity interest as its Fair Value for estate tax valuation on a Form 706, without considering liquidity discounts, the client may be harmed by being subjected to an overvaluation. This issue should also be considered when distributing decedent estate assets among heirs also. The realization of liquid return from a fund investment may take several years (even decades) or may never occur at all, even if underlying fund portfolio companies continue to operate. Sometimes, remainder portfolio companies' interests are distributed in-kind to fund participants, who subsequently become direct equity and debt owners of illiquid investments.

Valuation Complexities

Business valuation practitioners may find that their work product becomes the basis for an actual financial transaction in some cases, particularly in the field of wealth management. Whereas many valuation reports are used for internal purposes within an individual company or perhaps for loan collateralization considerations, valuations for portfolio administration are likely to be transacted upon in some fashion. Good examples of wealth management portfolio transactions are: the sale of a minority interest in response to a tender offer; asset division within a decedent estate or the sale of such assets to an outside party; or a proxy vote response for a proposed corporate acquisition event. These types of transactions expose a fiduciary asset manager to liability. Of course, business valuation determinations can be used as a basis for transactions of entire companies, but this is less common in reality. Most transacting parties in merger and acquisition scenarios are content to rely upon the opinion of investment bankers, lawyers, and business brokers. Since fiduciary asset managers are acting on behalf of their beneficiary clients, they are bound by duties of care, which are not always exercised by parties acting on their own behalf.

An interesting aspect of wealth management transactions in Private Placement assets is that the real-life effects of market illiquidity can be observed first hand. There have been a great deal of academic studies pertaining to the Lack of Marketability of illiquid assets, and the dispersion of the "discount" conclusions of these studies is quite wide. Some studies have claimed that marketability discounts may be as low as 2%.

A classic definition of "marketability" comes from The Encyclopedia of Banking and Finance, which defines the term "marketability" as follows:

"The relative ease and promptness with which a security or commodity may be sold when desired, at a representative current price, without material concession in price merely because of the necessity of sale. Marketability connotes the existence of current buying interest as well as selling interest and is usually indicated by the volume of current transactions and the spread between the bid and asked price for a security – the closer the spread, the closer are the buying and selling interest to agreement on price resulting in actual transactions. To look at it from the standpoint of a dealer maintaining the market, the closer his bid to current transactions and the smaller his markup as to asking prices, the larger the volume will be. By contrast, inactive securities that rarely trade or for which buyers have to be located or sales negotiated are characterized by large spreads between the bid and asked prices."

This theoretic sounding problem generally proves to be a royal nuisance in the real world. In the case of most marketable securities, investment portfolio assets may be converted into cash within a matter of days. In the case of Private Placement assets, even the most smoothly executed transaction will probably require months of work. Many assets will prove to be completely unsaleable. In the case of privately held stock, there may be transfer restrictions, which will discourage or preclude potential buyers. Common facets within partnership agreements and LLC operating agreements are rights of first refusal on the part of other current partners/LLC members or perhaps the incorporated entity itself. Most persons who are willing to invest in such types of investments do not want to make a serious time commitment to examining a potential investment, when they believe that it will be bought out after their issuing a purchase offer. Even in the case of unrestricted stock, sale transactions will generally drag out several months because of delays caused by legal formalities. These delays could lead to requests for escrow arrangements or transaction abandonment by the purchaser, assuming that one is located.

There are non-contractual barriers to marketability for Private Placement assets also, which most people do not realize. The most likely market for the sale of a Private Placement asset are other parties who are currently owners of the same investment. At least some of these parties have already contemplated exiting this investment also and have been unable to accomplish that goal. In the event that an asset manager is successful in marketing a Private Placement interest, other interest holders may attempt to "tag along" or supplant the asset manager's sale transaction. In the case of current interest holders who wish to continue with the investment, they may in fact express interest in purchasing the Private Placement offering, but perceive the selling party as having no recourse but to sell to an extremely finite pool of buyers. This can easily lead to a ridiculously low offering price, the acceptance of which might place a fiduciary asset manager in a position of breach of duty. It may well be discovered that persons with which an investor has partnered for years, or even other family members, may try to exploit sellers who are in a difficult position.

There may even be outright shareholder repression in some circumstances. I can recall several instances in which ridiculously low offers from current shareholders were declined in lieu of much higher offers from outside parties, which led to highly averse reactions and even refusals to honor stock transfers, on the part of the rejected offerors. Claims can be issued demanding rights of first refusal by current shareholders, even when there is no provision for such, because it is "owed" to them. Such instances can lead to the contemplation of expensive litigation and potentially years of transaction delays. Any academic study which concludes that the value impairment of Private Placement assets is a matter of minor significance is most likely not considering factors such as time value of money; legal costs; consulting costs; possible brokerage commissions; missed opportunity costs caused by the delay of sale proceeds; etc.

Correspondingly, valuation impairments for lack of control may be easily observed by Private Placement transactions. The market for non-controlling minority interests in an operating entity is far less robust than the market for controlling interests. Unfavorable treatment of minority shareholders and limited partners is commonplace, which is well known in the investment community. Many persons owning small blocks of stock receive little to no cash dividend return on their investment. A highly unfavorable scenario is that of an S corporation stockholder, who receives no cash distribution payouts from their holding but is subjected to passive income for their interest in a profitable company. Thus, the S corporation stockholder becomes legally liable for income taxation, without receiving any cash to fund said liability. This scenario is actually quite common for S corporation stockholders. Although, academic studies may indicate that S corporation investments are more profitable than C corporation investments, the reality is that entering into an S election, which is not within one's control, is in fact a highly risky commitment. The transactions of entire companies typically executed by investment bankers and business brokers are much easier to affect than transactions in small, minority interest investments, because of the existence of much larger pool of potential buyers.

So, How Can All This Be Avoided?

So, why would anyone want to manage a portfolio which contains Private Placement assets at all? Frankly, most asset managers do not. Several strategies are frequently employed to attempt avoidance of the administrative issues pertaining to Private Placement Assets, such as: business refusal, draconian asset management fee schedules, liability waivers, simply ignoring the portfolio assets, or even failing to list the assets as property. These efforts frequently fail.

If a fiduciary decides that it will no longer accept accounts with any type of Private Placement asset, how many business prospects has it preemptively eliminated? Such a trustee is hoping that accounts containing nothing other than marketable securities will be obtained as new business, therefore allowing the administration of large number of accounts with a minimal amount of effort and expense. Industry competition for accounts of this nature is fierce, and price discounting is inevitable. Moreover, accounts of such simple administration present the opportunity for a client to serve as its own trustee or appoint a non-corporate fiduciary, such as a lawyer. Clients are likely to perceive accounts of minor administrative difficulty as glorified brokerage accounts and wonder as to why fiduciary management fees should be paid at all. How does a fiduciary positively differentiate itself from competitors after stating that it does not have the expertise to administer a difficult account?

The imposition of additional fees for the administration of Private Placement assets is typical. After all, their administration does entail additional effort and liability exposure for the fiduciary. However, some fiduciaries have attempted to “scare away” existing clientele with Private Placement assets by presenting unreasonably onerous fee schedules. This strategy is problematic in that it may actually work and drive away customers. If an existing fiduciary account is really so difficult that it cannot be successfully administered, why was the business accepted in the first place?

Obtaining liability waivers of various sorts from trust beneficiaries is a common and probably the most sure-footed method of avoiding fiduciary liability exposure. Be careful though! Are these exculpatory contractual provisions really strong enough to hold up in court, if a harmed beneficiary files a tort suit against the fiduciary? Will the provisions excuse the fiduciary from complying with applicable government regulations, if a government agency becomes involved after bad publicity exposure?

Ignoring portfolio assets and/or hiding them from the account asset listing is the “whistling past the graveyard” approach. It might not even be legal. Some Private Placement assets are easily traceable by taxation authorities, particularly if they issue an annual tax reporting document, such as a Schedule K-1. If there is a disparity between activity on a trust's income tax filing and its statement activity, the matter should be obvious to a competent auditor. If a fiduciary simply fails to report Private Placement income taxation events on a trust tax return, taxation authorities should eventually notice the reporting failure, which could lead to penalties.

Ultimately, if one is in the business of acting as a fiduciary, Private Placement assets must be addressed. They are an inherent feature of a multitude of fiduciary asset pools and simply need to be dealt with. A fiduciary attempting to administer only the least complex accounts while receiving full fee remuneration is akin to an insurance company underwriting only policies, upon which claims will never be filed; it sounds great in theory, but will probably never happen.

Buried Treasure?

So, is there a silver lining to owning Private Placement assets or are they simply chronic difficulties that "come with the territory"? Let's consider some of the positive possibilities:

I) Potential for significant profitability

The reason for the popularity of private equity, venture capital, and other forms of early stage investment is that there is potential for unusually high returns on investment. Although only a minority of early stage investments come to full fruition, a well selected and diversified portfolio of investment assets can lead to capital gains realizations significantly higher than returns from marketable securities. In the case of fiduciary assets under management, the best example would be a corporate sale transaction of company in which the client has invested. The hypothetical financial asset (stock holding) could have been brought under fiduciary management at an artificially low carrying value, such as book value, and execute at a much higher value at a future date in the event of a merger / takeover transaction. Such a transaction will make the fiduciary asset manager look good, even if it had no active part in the transaction.

II) Reinforcement of client relationships

Administration of accounts with Private Placement assets can require significant client contact, particularly if those financial assets are holdings in family businesses. Competent and consistent dealings with clients on these matters can leave positive perceptions in the minds of the clients and dissuade them from selecting other fiduciaries. In this day and age of poor customer service, many clients will be flattered by the attention they are receiving from an astute investment manager. In recent years, banks have been losing ground to family offices for the roles of fiduciary asset managers of trusts. Attempts by banks to commoditize trust administration in order to streamline processes and eliminate employees has led to a decline in service quality, which is undoubtedly a contributing factor in the ascension of family offices. Serious scrutiny of private placement assets within a portfolio demonstrates that the fiduciary has a serious interest in the account and is adding credible value to the relationship. The extra time spent on these relationships might not enthuse an upper management focused on maximizing short-term profits, but will tend to bolster long-term viability of a wealth management product line.

III) Large asset values

Many Private Placement portfolio assets have a large weighting in client's overall net worth. How many investors have equity in their homes or other real property in excess of their marketable securities portfolio? Likewise, the value of successful small business interests can easily exceed the value of a client's marketable securities portfolio. If an asset manager refuses supervision acceptance of Private Placement assets, the value of these assets has been precluded from account inclusion.

IV) Higher fees

The possibility of extraordinary fee billing is quite realizable in relationships with Private Placement assets, by virtue of the fact that they are more work and responsibility. The administrative expenses of an efficiently run Private Placement asset management area can be more than offset by the extraordinary fees billed to clients for special services. For example: additional fees could be charged for income tax preparation for accounts with limited liability company and partnership interests; additional fees can be charged for real estate and privately held stock sales; fees can be charged for the vetting of potential Private Placement investments on behalf of the client; etc. Moreover, the direct expenses incurred for these actions, such as appraisal procurement, are generally billed directly to the client account anyway.

V) Improved marketing profile

A fiduciary's ability to effectively administer difficult accounts and resolve problematic situations will qualitatively differentiate it from competitors. Some of the most interesting anecdotes which can be told about financial asset management relationships originate from the handling of the unusual circumstances which can arise from Private Placement assets. Wouldn't a marketing presentation to a client about how your office was able to negotiate the sale of a business for top dollar be more compelling than talking about than your preferred mutual funds? If the only service being provided by an asset manager is to allocate capital within a predetermined investment platform, why would the client not simply take its business to a discount brokerage?

VI) Unexpected opportunities for exit may present themselves

Few investments mangers realize this fact, but opportunities for exits from Private Placement investments arise from time to time, if one is able to recognize them. There are frequently caveats in partnership agreements or LLC operating agreements which grant certain voting rights to individual investors. If these events require a unanimous vote or even a majority vote, the controlling stakeholder may find itself at the mercy of one or more aggressive minority interest holder and may consider buying said interest holder's ownership position. An example might be a change in a general partner or a significant operating asset liquidation. Events such as these do not occur frequently, and the ability to capitalize upon such events is contingent upon an asset manager's knowledge of the underlying contractual and legal structure of the investment, as well as its determination to negotiate on behalf of its client. However, a successful negotiation by an asset manager can result on a significant increase in investment asset capital.

Conclusion

Dealing with Private Placement assets is somewhat reminiscent of hunting for buried treasure on a beach with a metal detector. One will never know what will be unearthed, and when found you frequently don't want it. Sometimes it will be an interesting but valueless conversation piece; sometimes it is outright junk; sometimes, it is dangerous! However, sometimes the discovery will prove to be valuable, even if not immediately apparent. The biggest problem is being able to discern when a valuable discovery has been found and subsequently knowing what to do with it.

Here are some suggestions for persons charged with the task of handling Private Placement assets, either on their own behalf of for another party:

1) Figure out what it is and how it works

One of the most challenging aspects of dealing with a newly acquired asset is learning exactly what it is and how it operates. Reading governing legal documents is a daunting task for most people, but it is absolutely necessary to fully understand the issues. If one elects to refer this task to a lawyer, use a lawyer who has experience in corporate law. Learn what the business plan for the investment is and try to discern how well those objectives are being achieved. What assets are owned and are they being used properly?

2) Do not be afraid to make inquiries or to question management

General partners, fund managers, and company presidents and their colleagues on the board of directors prefer complacent investors. They generally get their wish. Partners and shareholders who unhesitatingly side with management frequently agree to vote for proposals which are not in their own best interest, or reauthorize the actions of a management organization which consistently fails to meet its performance objectives. Voting proposals which entail conflicts of interest, such as selling a company asset to an affiliate of a manager, are not unusual and should be thoroughly scrutinized. Many investment partnerships, such as private equity and hedge funds, provide bonuses for managers who attain performance objectives. However, one should note that the managers will always be paid some type of remuneration even if those objectives are not met, which provides management incentive to keep unproductive investments in operation or even retain an inordinately large amount of uninvested cash. If the business operation is profitable, don't be afraid to ask for a dividend.

3) Consider the taxation implications

"Pass through" taxation entities, such as partnerships and S corporations, are administratively difficult for individual taxpayers. A competent tax preparer needs to appropriately determine when passive income and passive losses may be offset against each other and records need to be maintained as to what passive taxation activity has been utilized and how it affects the tax cost basis of the underlying asset. Be absolutely certain to retain copies of taxation forms from these investments, no matter how old they are. Most wealth managers have trained taxation personnel to address these issues, but an individual investor may not be prepared to do so.

4) Document procedures

Procedural documentation is essential for any credible organization and will be a matter of import in the case of any litigious scenario. If someday questioned as to how an investment decision was derived, being unable to replicate the decision-making process or stating that an educated guess was made is not a credible defense. Government regulations state that Private Placement portfolio assets need to be reviewed and revalued on an annual basis. However, this process need not be overly cumbersome or expensive, since there is no requirement for the valuations to be USPAP (Uniform Standards of Professional Appraisal Practice) compliant. Documenting the requirements for these annual reviews is a factor in demonstrating that the asset manager is doing their job. Note that a higher standard of care should be considered in the case of taxable events or other more delicate transactions.

5) Comply with the procedures

This is not a joke. A great deal of cheating and short-cutting takes place in the world of wealth management, and this can end badly. Deliberately violating your own procedures, in order to cut expenses or avoid bothering with auditors and compliance personnel, is just as bad as not having procedures at all. Don't get caught doing this. If for some reasons, the procedures manual is not appropriate and does not make sense, change the procedures manual instead.

6) Always consider exit strategies carefully

The exit from a Private Placement asset is usually where the potential payoff can be attained. If some opportunity arises to liquidate operating assets and dissolve the operation profitably, it should be considered seriously. Likewise, a failing operation will probably continue to dilute in value over time, perhaps until nothing is left for equity interest holders. However, one should be careful about tender offers, particularly from management and its affiliates. Remember that some parties will always have more information about the investment than you do.

7) Don't forget that money can be made by buying, as well as selling

Wherever an illiquid asset exists, there is always someone trying to sell it. Some people will want to get rid of them at any price. If you are willing to make educated guesses about asset quality, take risks, and are willing to buy and hold investments for long time periods, the potential for payoff exists. Have fun with it!

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