

Wednesday, January 12, 2011

11:10am

*Discussion Materials – Not For Distribution*

# Making the Most of Your Co-investment Rights

*Richard B. Price*  
*R.B. Price & company, Inc.*  
[www.rbprice.com](http://www.rbprice.com)  
[rprice@rbprice.com](mailto:rprice@rbprice.com)

## What are Co-investment Rights?

- A contractual right to allow you, the buy-side M&A Intermediary, to invest side by side on an equal basis with a private equity sponsor to whom you have brought a deal. These rights are ***in addition*** to your cash fees.
- The right may be conditional, i.e. you don't have to buy the equity
- Usually 5% to 15% of the total purchase price
- You are paying ***no management fees or carry*** to the sponsor
- Under 30% of all M&A intermediaries even ASK for co-investment rights.

## Why Do You Want Them?

- They can provide you with more return than the “finders fee”
- Demonstrates “skin in the game” to the private equity sponsor
- Is “low cost capital” for private equity sponsors
- Potentially a “low cost investment” for the M&A Intermediary
  - Access a co-investment fund
  - Use 3rd party funds
  - Roll part of your fee
- Can potentially be a financial “home run” for the M&A Intermediary

## Possible Contractual Language

Co-Investment Rights. At each Initial Closing, Service Provider shall also have the right, but not the obligation, to purchase, upon the same economic terms and conditions as the Engager and its Affiliates, up to 15% of the Equity Securities purchased by Engager and its Affiliates, which co-investment rights shall be exercisable only to the extent Service Provider (or an affiliate of Service Provider which serves as the investor) is an accredited investor and shall be in the same proportion of common and preferred securities and other Equity Securities as is purchased by Engager and its Affiliates as of the related Transaction closing. To facilitate Service Provider's purchase of Equity Securities, Engager agrees to provide to Service Provider the same due diligence materials made available to Engager's investment committee or other such investment decision-making body. If, but only if Service Provider exercises the co-investment right described above at the Initial Closing, the applicable investment documents relating thereto will provide that if the Issuer thereafter issues, sells, grants or distributes any Equity Securities to Engager or any of its Affiliates, then Service Provider shall have the right, but not the obligation, to purchase, upon the same economic terms and conditions as Engager and its Affiliates, its pro rata share (based on its then ownership) of the Equity Securities being offered in such offering to Engager and its Affiliates.

\* The precise language you use should always be reviewed with your local counsel

## How Do You Get Them?

- ALWAYS DISCUSS co-investment rights with your private equity sponsor BEFORE sending your fee agreement
  - Emphasize that you are asking for the co-investment rights because they are an important part of your compensation for bringing valuable deals to private equity sponsors
  - NEVER send your fee agreement without first discussing 1) the percentage of co-invest that the private equity sponsor will permit and 2) when applicable, that the investment may be made by an affiliate using third party financing
- Almost all private equity firms will grant them subject to the approval of any third party financial partners
- But you have to ASK

## How Do You Overcome Objections?

- “We don’t want Outside Investors”
  - “But you have limited partners don’t you?”
  - “It is an important part of our compensation”
  - “Other private equity clients of ours allow us to invest”
- “We don’t want to share our due diligence materials”
  - “We will sign an additional NDA to make you comfortable”
  - “Would you share this with one of your LPs if they asked?”
- “It is too much of an administrative burden”
  - “You have to prepare reports and K-1s for your LPs don’t you?”
  - “We will administer our investment through a separately created LLC”
  - “We will pay your administrative costs”

## How Do You Finance Them?

- Self Financing
  - Your cash
  - Roll part of your finders fee
- Other Partners, e.g. family offices, institutional investors\*
- Co-investment Funds\*

\* Be transparent about your intention to use any third party financing sources at the outset - no surprises at closing!

## Illustrative Example of a Co-investment Transaction

