



3PM

THIRD PARTY MARKETERS ASSOCIATION

April 5, 2010

The Honorable Ed Hernandez
California State Assembly
State Capitol
10th and L Street
Sacramento, CA 95814

Dear Assembly Member Hernandez:

I am writing this letter to you today regarding Assembly Bill 1743 (“AB 1743”) introduced to amend the Government Code relating to the Political Reform Act of 1974. This letter is being submitted on behalf of the Members of the Third Party Marketers Association (“3PM” or “the Association”).

3PM believes that increased regulation and oversight are appropriate measures which will help monitor and prescribe the activities of placement agents, restore integrity to the investment decision making process in California and eliminate the inappropriate behavior that took place at one of California’s pension plans. That said we believe that as drafted, AB 1743:

- i) will create unintended consequences that are adverse to the best interests of the State of California and the beneficiaries of its public pension plans,
- ii) will not adequately solve the problems the proposed legislation attempts to address,
- iii) runs counter to what appears to be the emerging trend in addressing the issues regarding placement agents, fixers and finders which in our view, have incorrectly identified these parties as all performing the same function.

This letter will provide you with background on 3PM, identify and speak to a host of consequences which are important to consider when framing any legislation that will address what is a very real and legitimate concern, and suggest what we believe to be the appropriate framework for regulating placement agent activities, and eliminating inappropriate behavior in the investment decision making process in California.

The Third Party Marketers Association (3PM)

3PM was founded in 1998 to act as a trade group for placement agents. Today, the Association is comprised of 73 member firms. 3PM was formed to maintain a standard of excellence in the industry and to share information and ideas among independent sales and marketing firms. The Association helps to cultivate relationships and business opportunities among its members, and works to provide them with information and ongoing education about the investment management industry. 3PM's goal is to enhance our profession's standards, integrity and business practices. This is accomplished by advancing an ongoing agenda in the areas of regulation and compliance as well as adherence to the highest professional and ethical standards and best practices utilized throughout the financial services industry.

A typical 3PM member firm consists of 2 to 5 highly experienced investment management marketing executives with, on average, 10 or more years of experience of selling success in the institutional and/or retail distribution channels. The Association's members run the gamut in terms of the products they represent. Approximately 50% of the Association's members work as investment advisers with traditional separate account managers covering strategies such as domestic and international equity, and fixed income. In the alternative arena, members operate as broker-dealers and represent fund products like mutual funds, hedge funds, private equity, fund of funds and real estate. More than two thirds of 3PM's members work in both capacities.

3PM member firms that work with traditional separate account managers are typically registered under the investment adviser rules with the states in which they solicit business. Since the Association's members do not manage money they generally are not eligible to register directly with the SEC. The Association's members that work with Fund products deemed to be securities are either registered with FINRA as broker-dealers or work as Registered Representatives of an established broker-dealer to offer securities. Regardless of the structure within which 3PM members operate, they do fall under the scrutiny of one or more regulatory authorities.

For the purpose of this comment letter, and for consistency with the terminology utilized in AB 1743, we will use the term "placement agent" to encompass the myriad of terms used to describe paid intermediaries which include individuals referred to as third party marketer, solicitor, or third party intermediary. The term "investment manager" or "investment adviser" will be used to collectively include firms or individuals that oversee the management of client assets in a specified investment strategy. This group includes registered investment advisers as well as managers that do not legally require registration with the SEC, FINRA or other governing bodies. We have also provided a list of definitions for a number of terms used in the industry to describe the differing participants and their roles.

The Role of Placement Agents

Most placement agents provide investment managers with a comprehensive suite of value added sales and marketing services. Unlike the finders and fixers that were the principal focus of New York Attorney General Cuomo's inquiries, a placement agent's role is much more than merely arranging a meeting between an investment manager and potential investors. Most bona fide placement agents aid in identifying the most appropriate and suitable target markets for the fund manager's products, identify which distribution channels would be most effectively and efficiently utilized, and work with the fund manager to be as effective as possible in presenting the fund manager's story in those markets. In addition, most placement agents work with their clients to help them throughout the capital raising process, which typically includes helping fund managers put together the private placement memorandum, helping to develop with fund manager's investor presentations, helping to answer due diligence questionnaires and giving advice on governing document terms and conditions. This work is often driven by years of experience, and constant work with investors (both public and private) to understand the investors' programs and needs, so as to be able to present those investors with fund managers that are suitable to and satisfy the investors' interests and needs. This efficiency and effectiveness is of enormous benefit to both the fund manager represented as well as to the potential investor.

A small or emerging firm will generally not have the resources or background to recognize how to prioritize and approach the most likely prospective investors within a universe numbers in excess of 3,000 institutions. Conversely, institutional investors find value in knowing that products represented by placement agents will generally be more appropriate to that institution's investment program and strategy preferences.

Placement agents help fund managers define and position their products in what has become a very competitive market environment. As previously discussed, the typical scope of work that placement agents undertake is substantial. Placement agents do not just set up meetings; they create meeting agendas, organize the required materials, attend the meetings along with the firm's portfolio professionals, moderate the meeting, and help to ensure the clarity of fund manager's message as well as the investment objectives of each potential investor. Once the investment manager has been selected, the placement agent often continues to have an ongoing client servicing role which helps to facilitate communication between the fund manager and the investor.

3PM's Position

Recent events and the efforts to address certain corrupt actions have cast a shadow over what separates legitimate placement agents from the illegitimate ones. Over the past year, 3PM has worked tirelessly to differentiate the services offered by our members, who operate in a professional and ethical manner, from the unscrupulous few whose actions have tainted our industry. We have also tried to educate both the industry and broader audiences as to what a placement agent does and to articulate

that a placement agent's role is much more expansive than the roles played by introducing agents, finders, fixers and especially lobbyists. We strongly agree with the approach used by the State of California to take steps to correct and ideally to eliminate the pay-to-play issue through enhanced disclosure, and with certain aspects of its currently proposed-rulemaking, but without instituting a complete ban on placement agents.

3PM fully endorses a framework that increases the integrity of the investment decision making process and applauds the State of California for working towards achieving this goal. Despite our agreement with the intent of this proposed legislation, 3PM does have serious concerns with several areas of the proposal as it currently stands.

The following commentary is intended to provide insights and information regarding the current trends in regulation, the consequences of AB 1743 as drafted, and suggests changes that 3PM believes will enhance the bill, in ways that we believe are in the best interests of better government and the elimination of the practices that gave rise to this legislation.

Current Proposals Attempting to Eliminate Pay to Play Practices

As you are no doubt aware, the Securities and Exchange Commission (the "SEC") recently proposed a rule that would have banned placement agents from working with public pension plans. After substantial public comment, the SEC backed away from this approach, and has asked FINRA to take over the regulation of placement agents.

A number of states have also examined and acted on this issue, and have implemented policies and procedures aimed at ending this unscrupulous behavior. In New York, Attorney General Cuomo has led a charge to ban public pension plans from hiring investment managers utilizing the services of a placement agent. To date, the only New York plans that have banned the use of placement agents are the New York State Common Retirement Plan (NYCRF) and the New York City Retirement System (NYCERS). In fact, the ban implemented by NYCERS was a temporary ban and one that was intended to be overturned once the City could adopt rules and regulations to govern the actions of placement agents. In the past month, the NYC Comptroller's Office issued a proposed rule which will allow placement agents to participate in the investment process. Attorney General Cuomo also took his efforts one step further and has attempted to implement the Public Pension Plan Code of Conduct (Code of Conduct) which he asked more than 37 different State Governors to support. To date, no Governors have thrown their support behind Cuomo and his efforts to ban placement agents. Furthermore, Cuomo's goal was to have investment managers sign the Code of Conduct indicating that they would not retain the services of placement agents for any business involving public pension plans. While Cuomo has been successful in obtaining some signatures, it should be noted that every firm that signed this Code of Conduct did so as part of their settlement of other legal matters with the State of New York. New Mexico has decided to ban the use of placement agents. Illinois has banned contingent compensation arrangements, while a number of other states' public pension plans now require

comprehensive disclosure of dealings involving placement agents. Among these are North Carolina and Texas.

There have also a number of public pension plans that have written policies regarding the use of placement agents including CalPERS, the state of New Jersey, and the State of Connecticut.

While the approaches discussed are indeed diverse, we believe that the approach mostly likely to address the unscrupulous behavior that occurred and which have led to the drafting of AB 1743 are best addressed by a combination of placement agent regulation and laws aimed at regulating the conduct of public pension plan decision makers and influencers.

Placement Agents Benefit Small CA Pension Plans

Placement agents provide important services to investors who, like many smaller California public pension plans, do not have the time, resources or experience to review all potential opportunities that cross their desks. In order to be successful, placement agents need to conduct a thorough and comprehensive review of any fund manager it is considering representing. Not only must this review examine the fund manager's current performance, but it must include a detailed assessment of the product to ensure it will meet the investors' minimum investment criteria. Bypassing this step results in a failed business strategy for placement agents, both in the near and long term. Sales professionals rely on their reputations to garner new business. This naturally aligns with what is best for investors, and especially those that are constrained with regard to resources to review fund managers that come across their desks. Two of the key value propositions that placement agents provide are the initial vetting of fund managers, and the aligning of those qualified sponsors with investment programs that want what the sponsors are offering.

If investors believe that a marketer is credible about the products he or she represents, the investor will probably return the marketer's phone calls and respond to their emails understanding that they are likely to be introduced to quality managers. Alternatively, if a marketer consistently presents the potential investor with inferior managers, with undesirable investment strategies or uncompetitive performance, eventually, the sales professional will be viewed negatively and will be ignored by the prospect. As a result, many investors have come to rely on trustworthy placement agents to identify superior managers they would be interested in meeting.

Alternatively, several of the large pension plans who have the staff and infrastructure to implement open door policies, such as CalPERS and CalSTRS, believe that investment managers do not require their services because they are willing to meet with small managers. In keeping with CalPERS' policy mandates to invest in women and minority owned managers, placement agents help those managers to position themselves successfully so that they can rise above the noise, and get the attention of investors like PERS and STRS, even though they may not have the resources otherwise necessary to obtain commitments from this kind of investor. In such cases, placement agents provide a number of services

ranging from identifying the correct points of contact, scheduling meetings, evaluating and positioning the product, and creating and preparing marketing materials. All of these tasks are all extremely time consuming and necessary to win investment commitments. In small firms that cannot afford internal sales professionals these responsibilities are often handled by the Investment Team. Since time is a limited resource, more time spent working on sales and marketing means that less time is committed to managing clients' portfolios. From a fiduciary perspective, all investors should want to see legislation enacted that would ensure that portfolio managers have the time they need to do the jobs they were hired to do.

We believe that the limitations on fees currently embedded in AB 1743 will result in California public pension plans becoming investors of last choice because those fund sponsors that require the services of placement agent will find no agents willing to work for free. This result is contrary to what you are trying to achieve.

Women, Minority and Emerging Managers

In the investment industry, small managers are often referred to as emerging managers. At one time, the term emerging manager referred exclusively to minority and women owned investment firms. In recent years, the emerging manager universe has expanded out to include spin-out groups (that is, groups that had previously worked in other, often larger firms) and small firms regardless of the gender or race of their principals. Today, investors are even conducting searches in the alternative investment space and including both private equity and hedge fund emerging managers in their capital allocations.

California has a longstanding tradition of encouraging investment with and in minority and women owned and operated businesses. This holds true in the fund manager arena as well¹. In our experience many of these women and minority owned fund sponsors tend to be newer, emerging managers. As a result, they tend to lack the resources both to be able to effectively present themselves to investors and to pay advisory fees to placement agents on a non-contingent basis. As a result, it is our view that enacting AB 1743 as written would severely impair minority and women managers' access to capital from public pension plans based in California.

The Importance of Emerging Managers

The impetus for the growth and evolution of this sector has been investors' search for superior performance returns. Over time, many studies have shown that small firms have consistently outperformed larger firms. In one such recent paper published by Northern Trust in July 2009, titled "Insights on Emerging Managers; Emerging Managers Holding Their Edge Versus Elephants", Ted Krum, Vice President of Portfolio Management writes, "In six studies of emerging investment manager

¹ For example, the CalPERS AIM California Initiative Program

performance spanning 16 years of stock market history, Northern Trust has demonstrated that the smallest firms, collectively accounting for only 1% of institutional market share, enjoy a consistent advantage over industry leaders.”

In a 2008 article entitled “Successful Emerging Manager Strategies for the 21st Century”, regarding New York City pension plans, who actively invest in emerging managers, Thurman White, President and CEO of Progress Investment Management Company, LLC, offers the following definition: “In the public markets ‘emerging managers’ are defined as those managers with zero to \$1 billion in assets under management. In private equity, NYC defines ‘emerging’ as zero to \$400 million under management in first and second-time funds, while in real estate, ‘emerging’ is defined as zero to \$300 million in first and second-time funds.” 3PM believes that this definition is especially relevant in this instance not only because it corresponds to the beliefs stated above of one of the largest investors in the emerging manager space, but it also represents the opinion of a public fund, both of which focus on the exact constituency which the Commission’s proposed rule is intended to protect.

According to Altura Capital, a firm that specializes in the emerging manager universe, their Emerging Manager Information Platform shows that the total assets managed by the emerging manager universe, which is tracked by their database, totals \$233.2 billion, and represents more than 1,300 managers. This suggests an average of \$180 million of AUM per investment adviser. Of this total, \$71.2 billion is managed by 138 firms that are 50% or more owned by women, minorities or both. According to the website of Leading Edge Investment Advisers, a provider of multi-manager products utilizing emerging managers, the firm follows “over 1,200 asset managers in the traditional asset categories.”

Analysis of data gathered from Preqin and Hedge Fund Research (“HFR”) reveals that there are a significant number of emerging alternative managers comprise the current marketplace. According to Preqin, as of July 2009, more than 880 private equity funds were in the market raising capital. On average, these funds had a target fund size of \$260 million, a size classified in the industry as “emerging”. In the hedge fund arena, HFR estimates that as of the second quarter of 2009, there were more than 6,870 hedge funds and Fund of Funds in the market with less than \$500 million in assets.

In a study entitled “Venture Capital Funds Investing in Minority Owned Businesses: Evaluating Performance and Strategy”, conducted in part by the Ewing Marion Kauffman Foundation, William Bradford, Professor of Finance at the University of Washington said, “The way we see it, the minority business is growing three times faster than the primarily white (owned) businesses.”

We believe that these numbers generated by established resources are evidence of the overall significance of emerging managers, and especially minority and women-owned firms, in the current investment landscape a factor which is not apparently in account in AB 1743 as proposed.

If AB 1743 is enacted as proposed, the probability that these firms will succeed will be greatly diminished, because they will have far more difficulty accessing the capital they need to be successful.

These small firms frequently need the help of seasoned and experienced sales and marketing professionals who know what the investor community wants and needs, how to present that effectively, and who are motivated to obtain investor commitments.

Other Investment Managers Who Engage Placement Agents

In the private equity and real estate spaces, it is customary for many fund managers to launch new closed ended funds every two to three years. A significant number of these firms have chosen to retain the services of external placement agents because placement agents provide them with both better real time market data on the wants and needs of professional investors, with more efficiency than an internal full time investor relations staff can deliver.

According to Preqin as of mid-year 2009, there were 4,327 private equity and real estate funds. During the three year period ending 2008, roughly one half of these firms utilized the services of a placement agent.

This data is important for several reasons. First, it shows that the market place is very large and that there are a lot of funds seeking capital making it extremely competitive. Second, it proves the point that a significant number of private equity firms utilize the services of placement agents to help them navigate the investment industry. Finally, considering the extremely large number of potential private equity investments, it is unrealistic to assume that public entities will have the resources to allow them to effectively screen this large universe of managers without external assistance.

Preqin also tracked the level of private equity investing among US public pension funds. It reports that since 2006, public entities have made more than 2,455 separate commitments to private equity, real estate and infrastructure funds, totaling approximately \$484 billion. Overall, the Preqin data confirms that private equity investing goes far beyond the preferences of a few state entities. Rather, private equity comprises a central component of the investment programs of a majority of public pension plans. It also suggests that despite the allegation that the industry is rampant with imprudent and illegal behavior, the majority of funds have entered into transactions which are legal, ethical and proper. Further, despite the fact that more than 50% of private equity managers utilize the services of a placement agent, there are precious few that involved any sort of pay to play activities.

Aside from the unintended consequences of such legislation, the passage of AB 1743 will not address the root of the issue. State officials in California have said that when contingency payments are involved and can impact the decisions of public officials that the potential for corruption exists. We believe this is no more relevant to the investments industry than to any other industry, such as real estate, legal services, or even manufacturing. Notably, all of these industries derive revenue from performance-related compensation.

Although some of the people accused of being involved in corrupt activities were identified as placement agents, we believe that these operators are not “true” placement agents, but rather finders or fixers. Furthermore, all of the cases of pay to play activities identified to date also included “public officials” who were involved in the investment process. 3PM strongly believes that any proposed regulation should make a distinction between placement agents and those who are acting as finders or fixers. In addition, any legislation enacted should also include additional provisions aimed at preventing the kinds of recent corruption of public officials from occurring.

Prohibition on Contingency Fees

While the authors of AB 1743 are attempting to avoid banning placement agents from the investment process, we believe the result of their approach is likely to lead to unintended consequences as well. The current proposal would prohibit placement agents from accepting or agreeing to accept “any payment in any way contingent upon the defeat, enactment or outcome of any proposed legislative or administrative action.” If contingency fees are eliminated, placement agents would need to restructure their compensation structure to comply with this law. If AB 1743 is passed, the only acceptable form of payment would be in the form of a flat fee. As previously mentioned, most emerging managers lack the resources to pay a placement agent a flat fee or a “retainer” since much of their capital is allocated to the facilities and personnel required to manage portfolios.

If contingency fees were prohibited, we believe the consequences would harm both small and emerging funds and the public pension plans alike. First, since most small and emerging managers would have difficulty paying a fixed fee, their access to public pension funds would decrease. Second, many smaller public pension funds do not have the staff necessary to evaluate the wide array of investment options presented to them.

We believe the restriction on contingency fees will drive opportunity away from California. Placement agents working with more compelling managers will steer those managers towards other investors, creating an adverse selection process that will likely hurt the investment returns achieved by California public pension plans. Finally, since placement agents assist many investors by screening managers that are not a good fit for an investor’s portfolio, a bias will likely develop for California pension managers whereby public pension funds will either continue to invest with existing managers, or place bigger amounts of money with managers because they do not have the bandwidth to properly assess and evaluate new offerings, resulting in an investment bias toward larger funds, which we believe runs counter to prudent investment strategy.

Contingent compensation arrangements help to align interests among all of the parties involved in the fund manager selection process. Placement agents need to make good manager choices, or they won’t be successful or get paid. Managers win because they only have to pay a placement agent based on the results the placement agent is able to achieve. This type of fee structure also assists investors.

Placement agents serve as a filter that weeds out managers not worthy of investment and narrows down the universe of managers which they need to review.

The manner in which placement agents are currently compensated is no different than any success-based compensation program. Contingency fees are used in a variety of industries as a way to incentivize service providers, align the interests of various parties and share the risks involved in processes with uncertain outcomes. Throughout the United States, contingent fee arrangements are used to compensate lawyers, real estate agents, brokers and sales professionals. They are also commonplace in the investment arena including many California state government agencies, where they are used as part of the compensation package for portfolio managers, investment analysts, traders and of course for sales professionals. The critical point for consideration should not be focused on the form of the payment, but rather on three key elements: i) knowing who is being incented, ii) making sure that the person or organization is legitimate and is providing an actual service, and iii) providing transparency as to how any such payment could influence investment decisions.

Often contingency fees are used by pension plans and other investors, in the form of performance fees, to try to garner high returns from the investment managers they hire. The thought behind this kind of fee structure is that the more incentive the portfolio manager has to generate returns the harder he or she will work to attain that stated goal, creating a win-win situation for all parties involved.

It should also be noted that when a contingency fee is paid to a placement agent, the fee is not paid by the investors, but rather by the investment manager retaining the placement agent's services. This approach is no different than the compensation an internal sales professional would receive. In fact, by hiring a placement agent, an investment manager could actually save money by reducing the overhead costs allocated to full-time employees. These funds could then be allocated to other areas of their businesses which could help achieve higher investment returns.

Sales and marketing are essential to growing most businesses regardless of industry. The cost for this imperative resource is generally chalked up to the cost of doing business. We believe by prohibiting contingency fees, the State of California is in fact dictating the manner in which an investment manager can run their business, simply because a handful of political officials acted badly.

Without contingency fees, investment managers will need to find other ways to grow their assets or risk going out of business. Some may resort to unethical approaches and use loopholes to get around the rules. Managers, who "game" the system by finding alternative ways to get paid higher fees if business is awarded, will be further injuring the integrity of the investment process rather than improving it.

We believe AB 1743 favors larger funds, funds capable of affording to allocate resources to internal infrastructure. For instance, AB 1743 provides an exemption to "an employee, officer, director, equity holder, partner, member, or trustee of an external manager who spends one-third or more of his or her time, during a calendar year, managing assets controlled by the external manager." This exemption is

problematic not only to the investment management firm, but also to the pension plans hiring them. This will result in a natural bias toward larger funds which can afford such an allocation of resources, and runs counter to many CalPERS policies which encourage the pension plan to invest in minority and emerging managers. For smaller firms, unable to hire dedicated sales personnel, portfolio managers will now have to split their time between managing portfolios and their new sales and marketing function. It is likely that they will also need to spend time learning how to market their products, identifying the appropriate contacts, scheduling meetings, as well as creating presentations and other collateral materials required by the sales process, all of which will take away from their primary responsibility, to manage the monies given to them to achieve maximum returns. As fiduciaries, pension plans should want to see their portfolio managers spending as much of their time as possible on investments, rather than travelling around the country attending sales meetings. But whether they realize this or not, this is the behavior AB 1743 will engender.

Placement Agents are not Lobbyists

Section 82039 of the California Government Code defines a lobbyist as an individual who is compensated for directly communicating with a qualifying official when trying to influence legislative or administrative action. (See full definition at the end of this letter.) Placement Agents are not lobbyists. Such a comparison is undeniably inaccurate and assumes that every Placement Agent has connections with the people who are in a position to influence investment decisions whether they are politicians or the internal staff members of a public pension plan or that we are in a position to contribute significant funds to influence the process. Our mission is not to adversely influence the decision makers but rather to help present the managers we represent in a way that best demonstrates its investment capabilities. In order for us to be successful, these managers need to receive fair and equal consideration and participate in an investment environment where awards are made on the basis of merit rather than undue influence. No one wants to restore integrity back to the investment process more than the Placement Agents who have been labeled as the notorious villains responsible for causing the pay-to-play issues.

Placement Agent Registration and Oversight

3PM has long recognized the need for regulatory oversight and additional transparency in the financial industry and we believe that the investment process can be strengthened by mandating additional disclosure and regulation. In this respect, we would support the implementation of new legislation which included registration requirements for placement agents similar in nature to those currently used for lobbyists.

Given the inherent differences in the roles of a placement agent and a lobbyist as well as the fact that the constituencies who hire each of these professionals is distinct, we believe that the process should be modified to effectively enhance transparency and the usefulness of registration and disclosure.

We believe that the registration and disclosure process should be modified so that it would correctly reflect the information relevant to placement agents. Simply using existing forms which may not apply to placement agents will only lead to confusion in the process. The current system was designed to add transparency to the process by giving the public access to information relating to registered lobbyists and their activities. Adding placement agents to this site would not promote clarity, but would rather lead to misunderstandings regarding the information provided. We believe that employees of the State who are using this system to ensure corruption is not occurring would be better served if they could identify the exact nature of payments that are disclosed through this system.

3PM believes that an ethics course could be an important registration enhancement so long as the course requirements are specific to the work and responsibilities of placement agents, and specifically in identifying situations where conflicts of interest are likely to occur. Under the current framework, the ethics training is only provided in the Sacramento area, making it extremely difficult for those living and working outside this geographic region to reasonably gain access to it. Since this course is a registration requirement, many Placement Agents would have to travel a considerable distance to get access to the training if they wanted to conduct business with any of the State's public pension plans. Alternatively, we believe that the ethics training should be offered in an on-line format or could be made available in testing centers around the country.

3PM believes that it would be more than reasonable to require placement agents to fully disclose any contributions made or gifts given to or at the request or suggestion of any public official or other person with the ability to influence the investment process. Members of the Association would even go so far as to prohibit their employees from making direct or indirect contributions to any official who partakes in the investment decision making process.

The Impact of AB 1743

While simple in approach, we believe that the authors of AB 1743 miss the mark by adding a sentence to an existing rule as the way to cure the ills that have resulted in the incidents of corruption that have recently been uncovered. Simply stated, we believe that rigorous registration, qualification and disclosure requirements will serve the interests of all constituents in this arena far better than the seemingly simple approach contemplated by AB 1743. The current approach undermines the important role that placement agents play both for investors of all kinds and for a broad swath of investment managers, and fails to address the real underlying problem at work here. This bill will not only have a negative effect on placement agents, but also on a variety of constituencies which include public pension plan sponsors and a variety of investment managers including women, minority and emerging managers, who, given their size often utilize the services of a placement agent.

3PM Recommendations

While we are in agreement that change is necessary and appropriate, we are not convinced that AB 1743 will facilitate the changes needed to ensure that corruption is eradicated from the investment process. We believe that the proposed bill will not only prove ineffective but will also be counterproductive. As such we recommend the following amendments be made to the current version of the proposed legislation.

In order to promote transparency a new policy specific to placement agents should be created. The legislation should contain registration and disclosure requirements appropriate to the nature of the placement agent business rather than trying to use an inherently political model (lobbyists) in a financial setting. These disclosure and registration requirements should include:

- A requirement that all placement agents be registered with FINRA;
- All professionals employed by or working as placement agents have and maintain appropriate registrations with FINRA;
- A requirement that all placement agents register with the state of California if they wish to do business with any public pension plans, and make quarterly reports regarding their activities involving any California based public pension plans;
- A requirement that all placement agents offer and provide a broad range of services that extends beyond mere introductions. Specifically, these should services that include the preparation of marketing materials and strategy pieces, due diligence questionnaire preparation, and the like, and that all placement agents be required to prove that they work with a broad range of investors;
- A requirement that all placement agents and their compliance officers understand and agree to abide by a set of ethical standards established by the state of California;
- A prohibition on all political and charitable contributions and other gifts by placement agents and their immediate family to any California domiciled pension plan or to any person, organization or other entity that could directly or indirectly influence any investment decision by such a pension plan;
- A requirement to report all gifts and contributions made by placement agents and their immediate families so as to assure the State of California that no untoward or indirect attempts are made to circumvent the requirements described above; and

- Full disclosure of all fees and other consideration paid to placement agents by investment managers associated with capital committed by any California public pension plans.

We are convinced that legislation alone will not be enough to fix what is broken. The State of California must go forward and make changes not only to the way placement agents operate, but must also address deficiencies in the way that public officials are regulated when they are involved, directly or indirectly in an investment decisions of any public pension plan. New policies and procedures that can effectively monitor the conduct of all parties and can appropriately identify individual interests that may influence investment policies and practices are also needed. Any changes implemented should include enough transparency to identify those who receive compensation from investment decisions and related activities and provide disclose relating to who is paying such compensation. Finally, a system of oversight must also be put in place along with harsh penalties for those that engage in corrupt and illegal behavior whether they are placement agents, pension plan staff or public officials.

If you have any questions or comments regarding any of the information contained in this letter or would like to discuss any of these comments in further detail, please feel free to contact me directly by phone at (212) 209-3822 or by email at donna.dimaria@tesseracapital.com.

Thank you in advance for your consideration.

Regards,



Donna DiMaria
President of the Third Party Marketers Association

For more information on 3PM and its members, please visit www.3pm.org

CC: Honorable Warren Furutani, Honorable Jim Beall, Honorable Brian Nestande, Honorable Alberto Torrico, Honorable Paul Fong, Honorable Anthony Adams, Honorable Bill Berryhill, Honorable Joe Coto, Honorable Tony Mendoza, Honorable Lori Saldana, Honorable Sandre Swanson, Honorable Audra Strickland, Honorable Marty Block, Honorable Ted Lieu, Honorable Bob Blumenfield, Honorable Joan Buchanan, Honorable Fiona Ma, Honorable Anthony Portantino, Honorable Lou Correa, Honorable Bill Lockyer, and the CalPERS Board Members Rob Feckner, George Diehr, John Chiang, Patricia Clarey, Dan Dunmoyer, Henry Jones, Priya Sara Mathur, Louis J. Moret, Tony Oliveira, Kurato Shimada, J.J. Jelincic, Debbie Endsley

Definitions

Third Party Marketer - An unaffiliated firm which enters into agreements with investment managers to provide sales, marketing and client service. The term is general and is not specific to any one asset class or product offering. Most Third Party Marketers are registered with the FINRA and/or the States in which they conduct business.

Placement Agent: A company that specializes in finding investors that are willing and able to invest in private placement funds such as private equity and real estate. Most Placement Agents are registered with FINRA

Finder or Fixer: Someone who finds, introduces and brings together parties interested in a specific business transaction. Generally the parties themselves negotiate and consummate any relationship or agreement. A finder: (1) locates, introduces or refers any person to an issuer; (2) does not give investment advice about the advantages or disadvantages of an investment; (3) does not participate in any presentations or negotiations about any material term of an investment; and, (4) does not receive compensation based on the amount of any investment made but may otherwise receive compensation. Generally is not registered,

Lobbyist: A person, acting for a special interest group, who tries to influence the introduction of or voting on legislation or the decisions of government administrators.

Lobbyist as defined by California Government Code Section 82039: Lobbyist (a) means any individual who receives two thousand dollars (\$2,000) or more in economic consideration in a calendar month, other than reimbursement for reasonable travel expenses, or whose principal duties as an employee are, to communicate directly or through his or her agents with any elective state official, agency official, or legislative official for the purpose of influencing legislative or administrative action. (b) For the purposes of subdivision (a), a proceeding before the Public Utilities Commission constitutes "administrative action" if it meets any of the definitions set forth in subdivision (b) or (c) of Section 82002. However, a communication made for the purpose of influencing this type of Public Utilities Commission proceeding is not within subdivision (a) if the communication is made at a public hearing, public workshop or other public forum that is part of the proceeding, or if the communication is included in the official record of the proceeding.