

# An Introduction to Structured Trust Acquisition Companies

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## Private Equity and Public Dollars

- As of October 18, 130 companies have completed initial public offerings raising total proceeds of \$27.6 billion in 2006. Last year, 194 companies completed initial public offerings raising total proceeds of \$34.0 billion. (Source: <http://www.IPOHome.com>)
- As of October 8, private equity funds have closed 770 control-stake transactions for \$181 billion this year. In 2005, private equity funds closed 840 control-stake transactions for \$198 billion. (Source: <http://www.buyoutnews.com>)
- The market is looking for a way to marry these concepts so that private equity can access public dollars.

## Accessing Public Dollars

- Private equity fund investing has historically been the exclusive province of wealthy investors.
- Private equity funds have largely been structured as limited partnerships (or limited liability companies), with the investors as the “limited partners” or “LPs” and the private equity manager as the “general partner.”
  - Inaccessible to most market participants
  - Each LP of a private equity fund must generally be an “accredited investor”
- The primary ways for private equity managers to access the public capital markets are through:
  - Business development companies (“BDCs”)
  - Special purpose acquisition companies (“SPACs”)
  - Structured trust acquisition companies (“STACs”)
  - Public offerings in Europe i.e. KKR’s Euronext IPO

## Publicly Traded Private Equity Investment Vehicles

- No perfect fit. Each primary vehicle for taking private equity public has advantages and disadvantages.
  - BDCs: Control and Non-Control Investing through a related vehicle.
    - 1940 Act restricts compensation and leverage
  - SPACs: One and done.
    - Short lifespan for promoter who typically exits after one business combination
  - STACs: What's a STAC?
    - Innovative new structure, but not yet widely known in the market
    - Can serve as a perpetual SPAC or buyout fund effecting unlimited business combinations
  - Initial Public Offerings in Europe

## Comparing Investment Vehicles

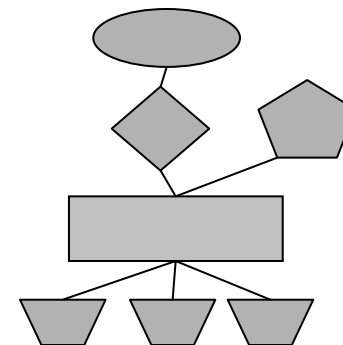
	<u>STACs</u>	<u>SPACs</u>	<u>BDCs</u>
Investment Company Act Compliance	No	No	Yes
Management	To date only external	Internal	Internal or External
Investment Objective	Long-term control- stake ownership of operating companies.	Short-term — limited to one business combination	Long-term control or non-control ownership.
Exchange Listings	NYSE NASDAQ	AMEX	NYSE NASDAQ AMEX
Pass-thru vs. Entity Taxation	Pass-thru	Entity	Pass-thru

## Comparing Investment Vehicles (Cont'd)

	<u>STACs</u>	<u>SPACs</u>	<u>BDCs</u>
Business Combinations – Shareholder Approval	No	Yes	No
Operating/ portfolio companies	May IPO with or without operating businesses	Business combination always subsequent to IPO.	May IPO with or without portfolio companies.
Executive compensation	Management fee, distributions on management interests	Usually no compensation until initial business combination	Management fee
Financial Reporting	May consolidate financials.	N/A	Must report on each portfolio investment.

## What are Structured Trust Acquisition Companies?

- Since December 2004, two Structured Trust Acquisition Companies, or STACs — Macquarie Infrastructure Company Trust and Compass Diversified Trust — have consummated IPOs, raising more than \$700 million in equity capital.
- Similar arrangements:
  - DB Commodity Index Trading Fund
    - Trust investing in exchange-traded commodities futures
  - Barclay's iShares Commodity Index Trust
    - Investing in long positions for futures contracts
  - Equity Gold Trust
    - Trust holding gold bullion



## A Comparison of STACs

	<u>Macquarie</u>	<u>Compass</u>
Size of Offering	535,000,000	202,500,000
Sector	Infrastructure Businesses	No specified sector
Payments to Manager	<ul style="list-style-type: none"> <li>▪ Management Fee</li> <li>▪ Performance Fee</li> </ul>	<ul style="list-style-type: none"> <li>▪ Management Fee</li> <li>▪ Profit Allocation</li> </ul>
Exchange Listings	NYSE	NASDAQ
Use of IPO Proceeds	Purchase-affiliated operating companies	Purchase-affiliated operating companies
52 Week Range of Stock Prices (IPO price)	\$23.84 - \$35.23 (\$25.00)	\$12.79 - \$16.98 (\$15.00)

## What are STACs?

- STACs implement innovative organizational and structural features to achieve specific business, operational and financial objectives.
  - *Flexible Structure*
    - Investment objective
    - Management
    - Operating companies
  - *Alignment of Interests*
    - Profit-sharing arrangements can be customized and implemented to align management's interests with those of the public investors through operating agreements at the holding company level.

## What are STACs? (con't)

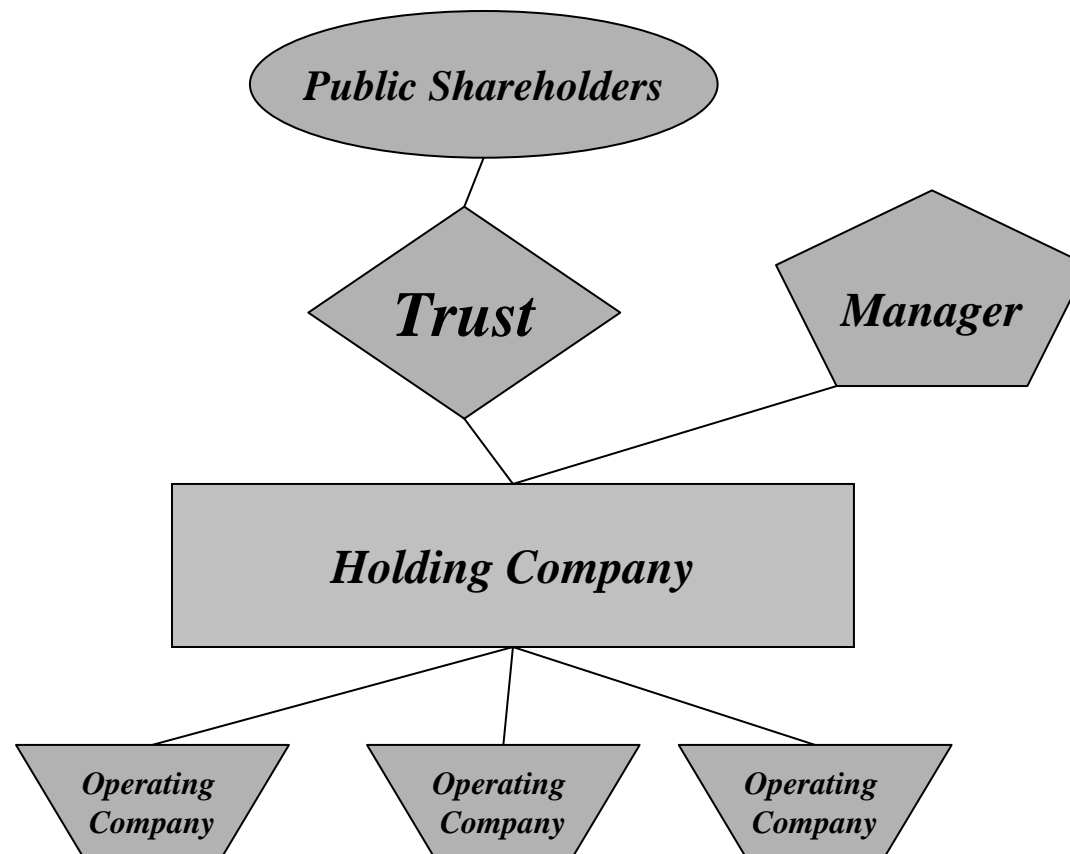
### – *External Management*

- STACs outsource management pursuant to “global” management services agreements that provide for the calculation and payment of a single management fee. This structure provides greater transparency to public investors than traditionally complicated compensation packages for corporate executives.

### – *Partnership Taxation*

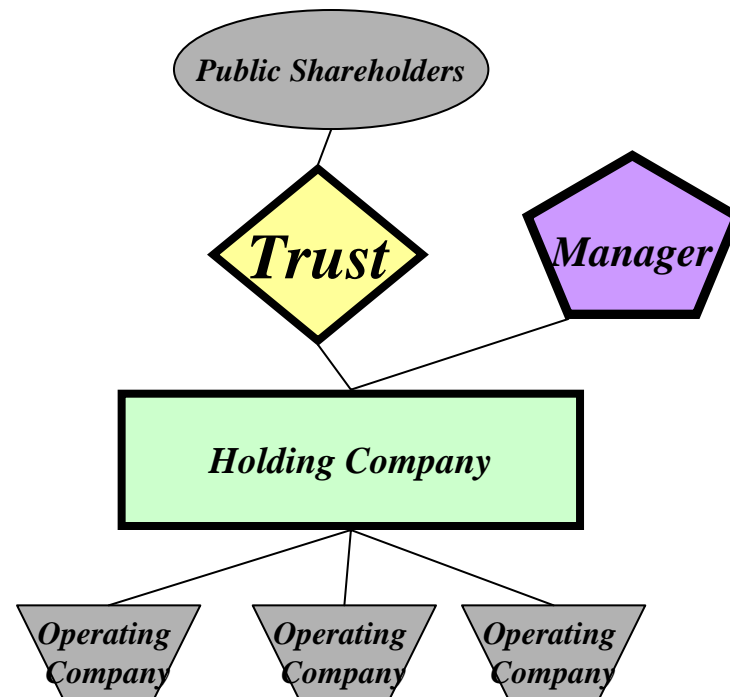
- STACs provide “pass-thru” or partnership taxation and, therefore, avoid entity level taxation with respect to income and gains received from the control-stake businesses.
- STACs also benefit from simplified, market-friendly, reporting of investment income to the public investor.

## The Structure



## Structural Overview

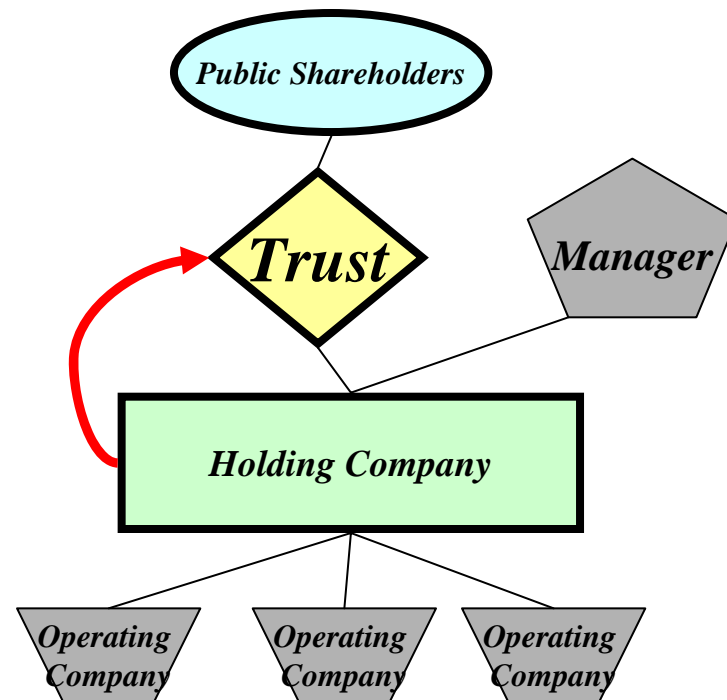
- STACs are structured using:
  - a newly formed Delaware statutory trust,
  - a Delaware limited liability company, and
  - a manager which can be a corporation, limited partnership or limited liability company.



## Structural Overview

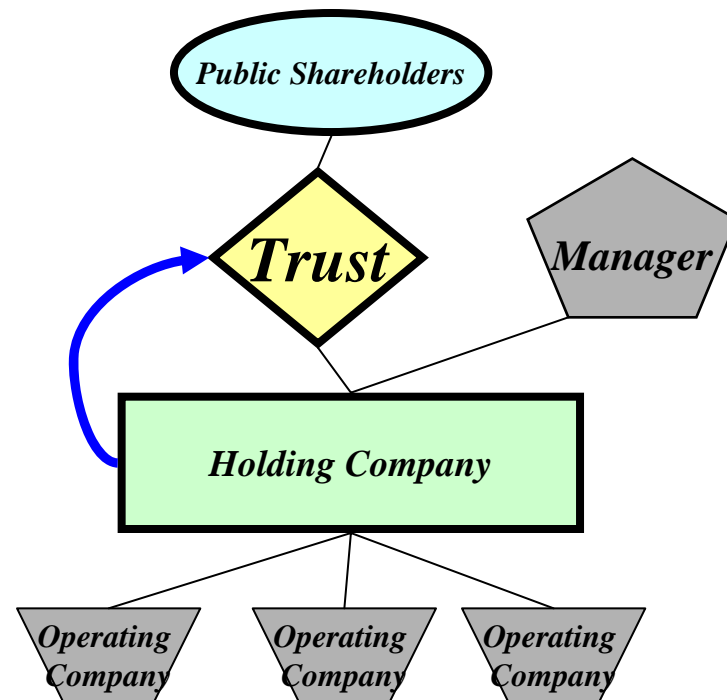
*The following are typical elements of STACs:*

- The Trust will own interests in the Holding Company. These interests will comprise the Trust's sole property underlying the trust's publicly issued shares.



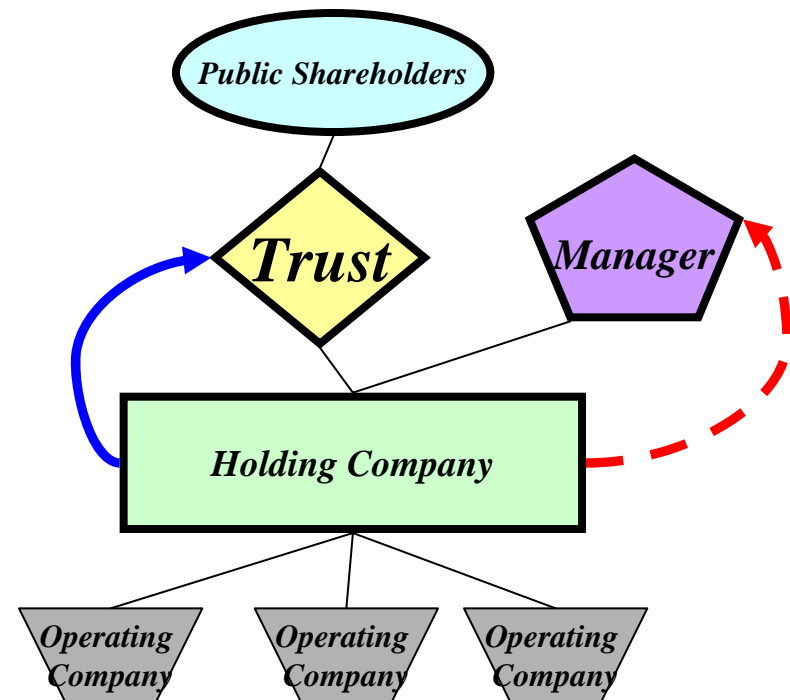
## Structural Overview

- The Holding Company will have one or more classes of interests, one of which will be held by the Trust.



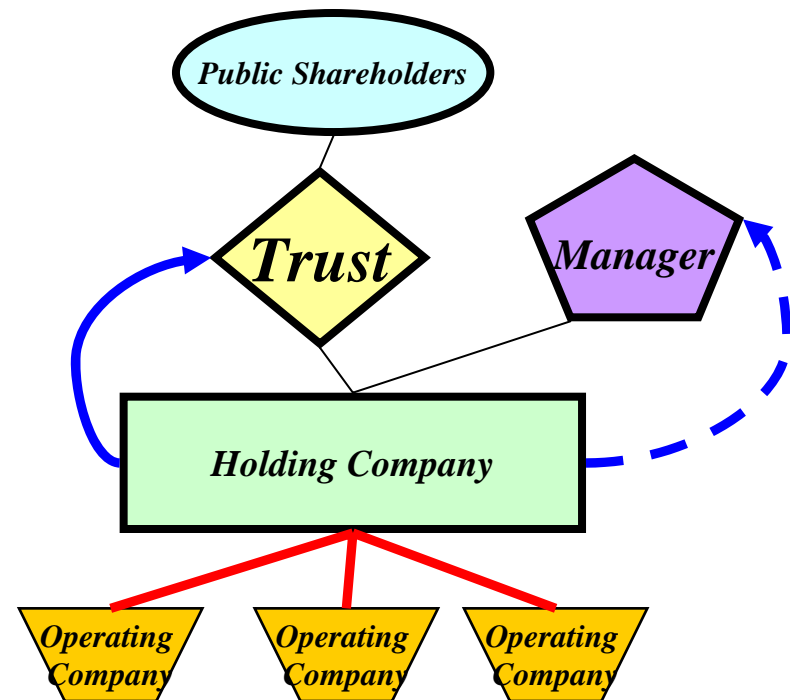
## Structural Overview (con't)

- The Holding Company will be externally managed.
- A second class of the Holding Company's interests may be issued to the external manager as a profit-sharing arrangement.



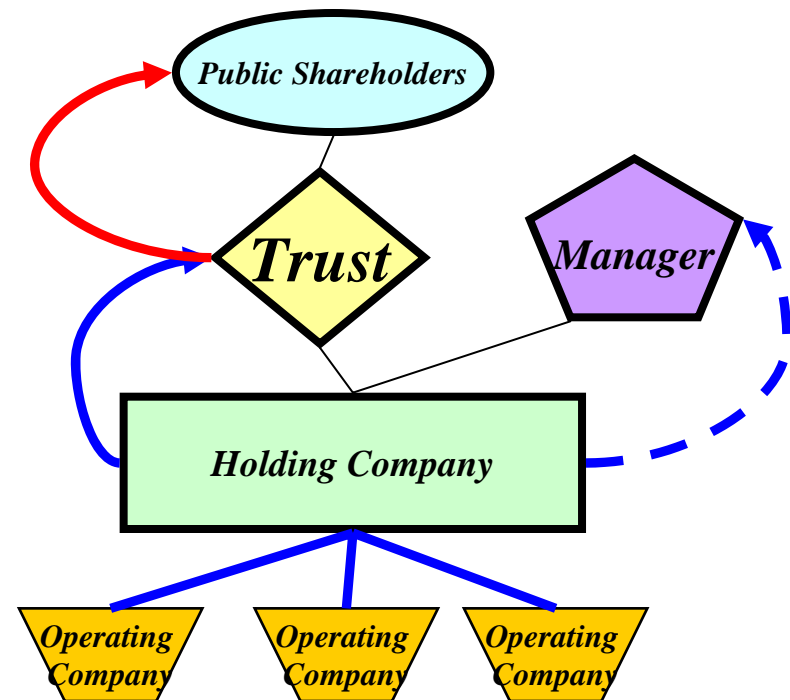
## Structural Overview (con't)

- The Holding Company will own controlling interests in one or more operating businesses.
- The Trust will hold no interests in such businesses.



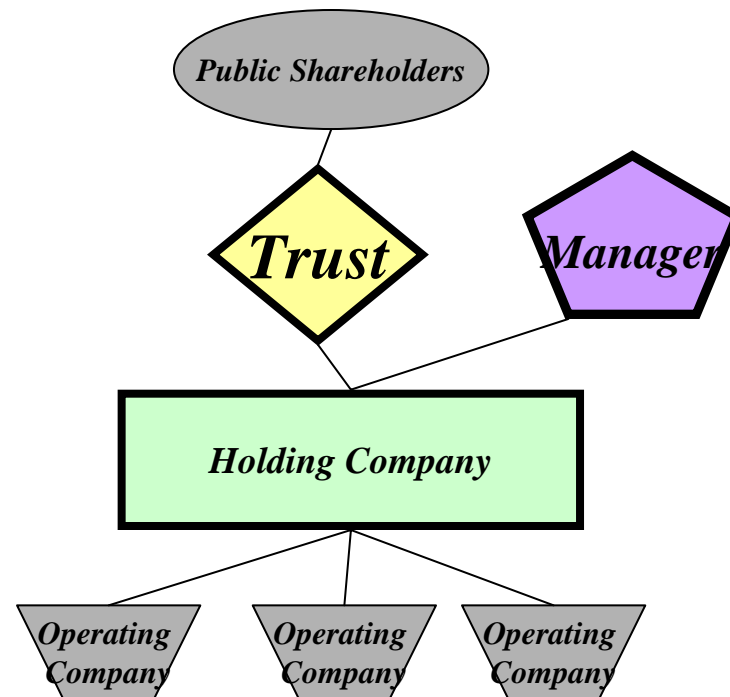
## Structural Overview (con't)

- Pursuant to an IPO the company and the Trust will issue the shares of the Trust to Public Shareholders.
- Trust and Holding Company usually joint registrants with trust shares and interests of Holding Company registered as public securities.



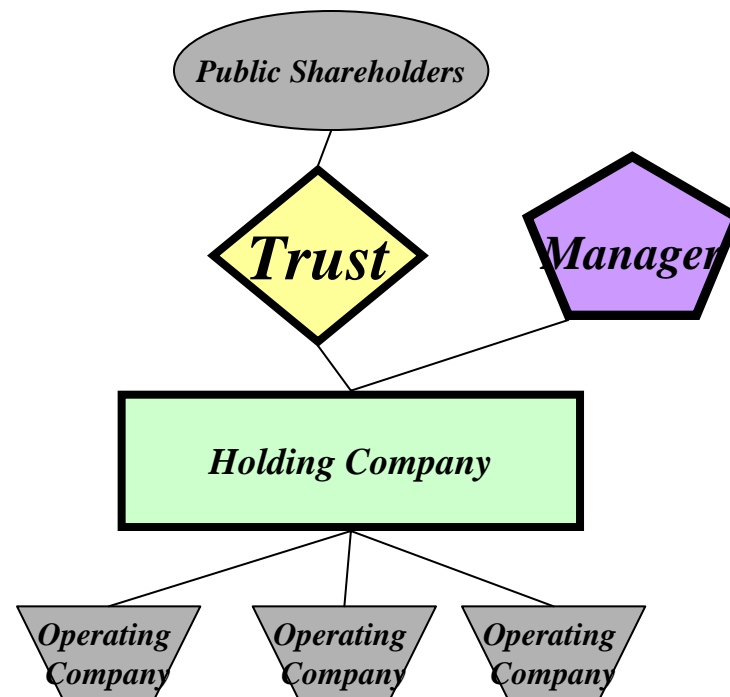
## Tax Matters

- Structural issues
  - Factors in trust investment trust/  
Favor trust
  - Partnership/ single member LLC
  - Publicly traded partnership: qualifying income exemption
- Goal: No entity-level tax



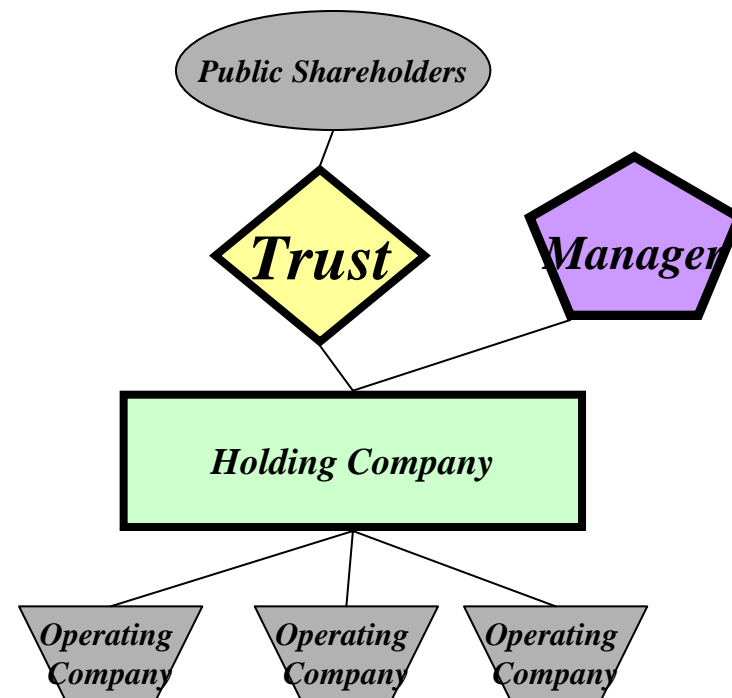
## Tax Matters

- Reporting issues
  - WHFIT market friendly reporting.
  - Partnership reporting



## Tax Matters

- TAX treatment
  - Investor as “partner” for tax purposes
  - Manager as “partner” for tax purposes

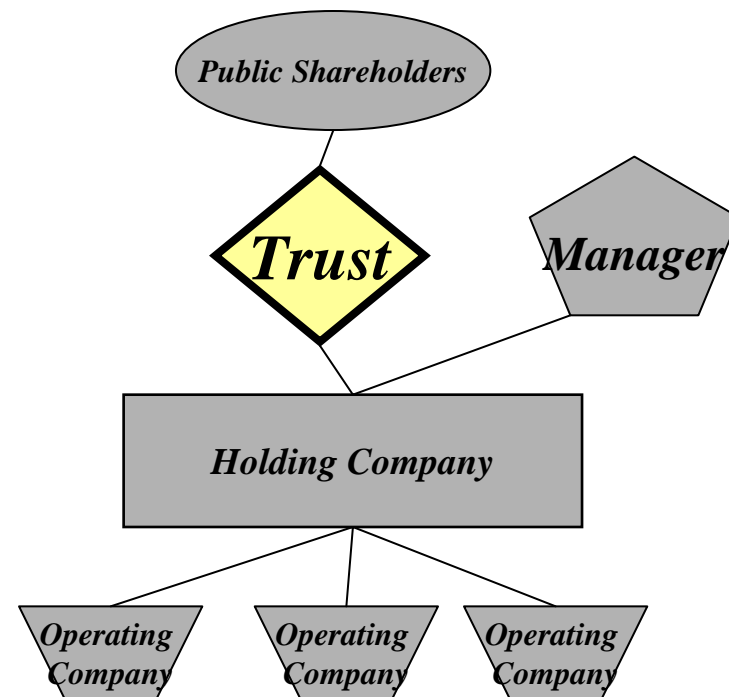


## Governance and Compliance Issues

- **Governance**

- Trust

- The board of trustees has mostly ministerial duties. Trust must vote its interests in the Holding Company in the same proportion as the vote of public holders of the Trust's shares.
    - No officers or employees.

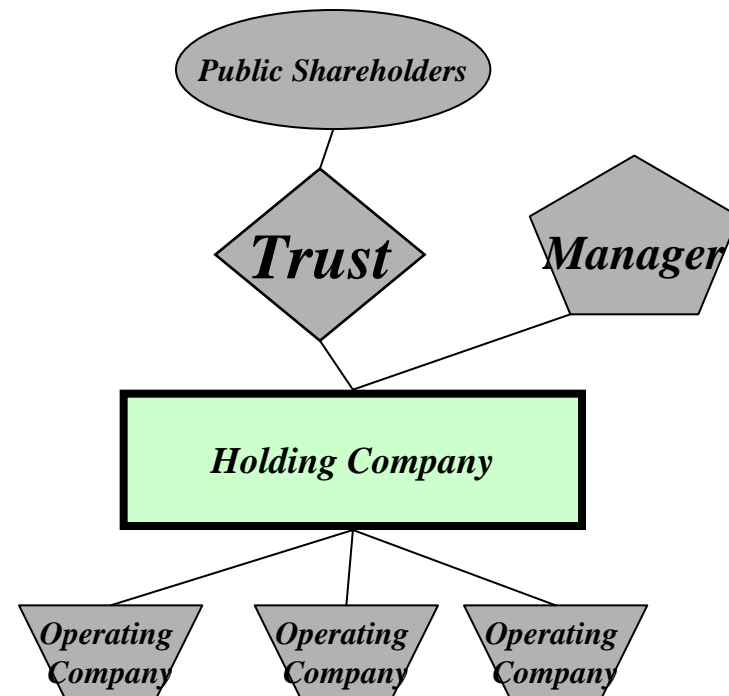


## Governance and Compliance Issues

### ■ Governance

#### – Holding Company

- Board of directors plays important role in governance.
- Charters and corporate policies adopted at this level.
- Determination of management fee pursuant to management services agreement.
- Determination of disbursements from the holding company.

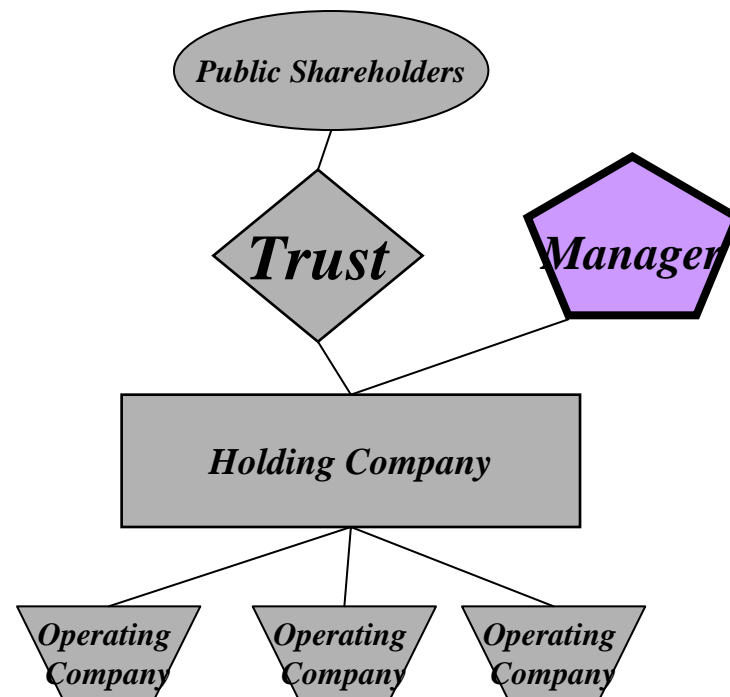


## Governance and Compliance Issues

- **Governance**

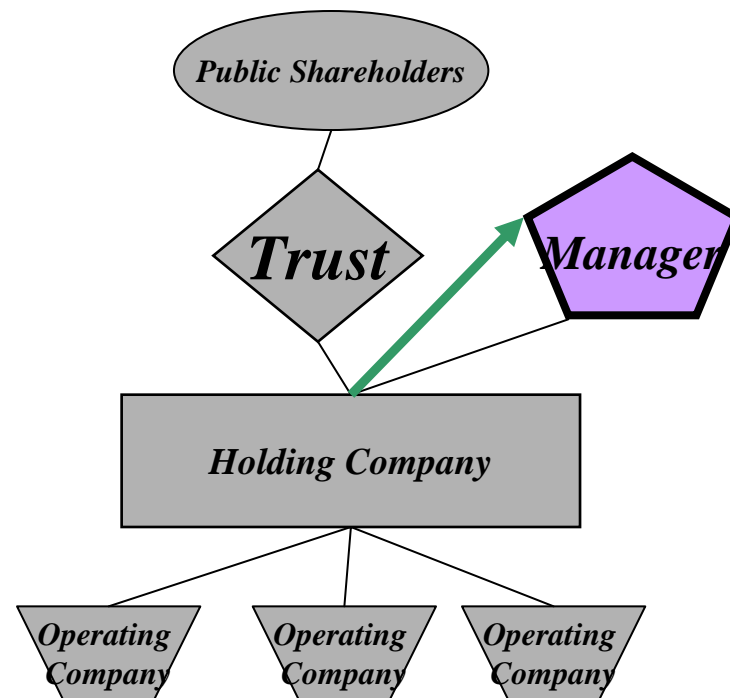
- **Manager**

- Manage day-to-day operations of the holding company. Evaluate acquisition opportunities. Monitor business and operations of operating companies.
    - May also manage day-to-day operations of operating companies pursuant to management services agreements which may be partially offset by the manager's agreement with the Holding Company.



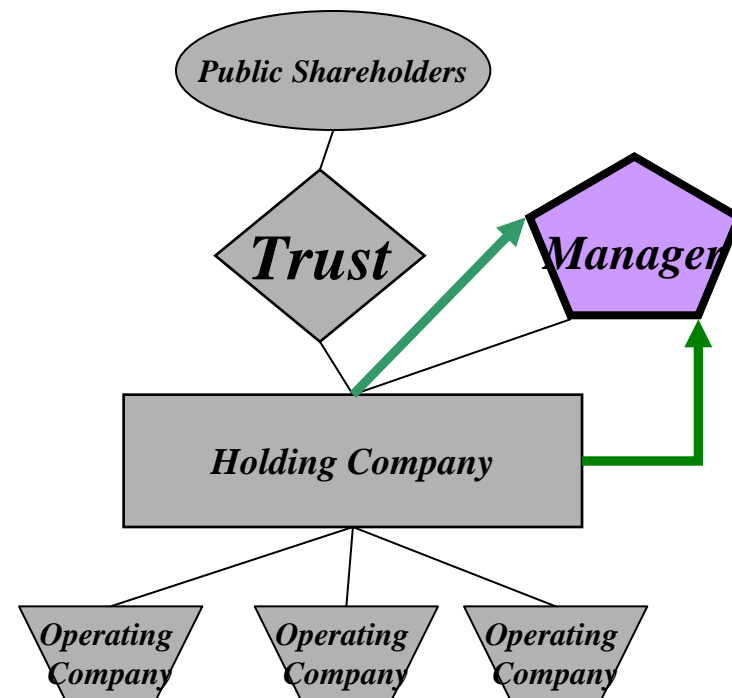
## Payments to the Manager

- The Manager may receive payments from the company or the operating businesses in the form of:
  - Management fees pursuant to management service agreement with the Holding Company.



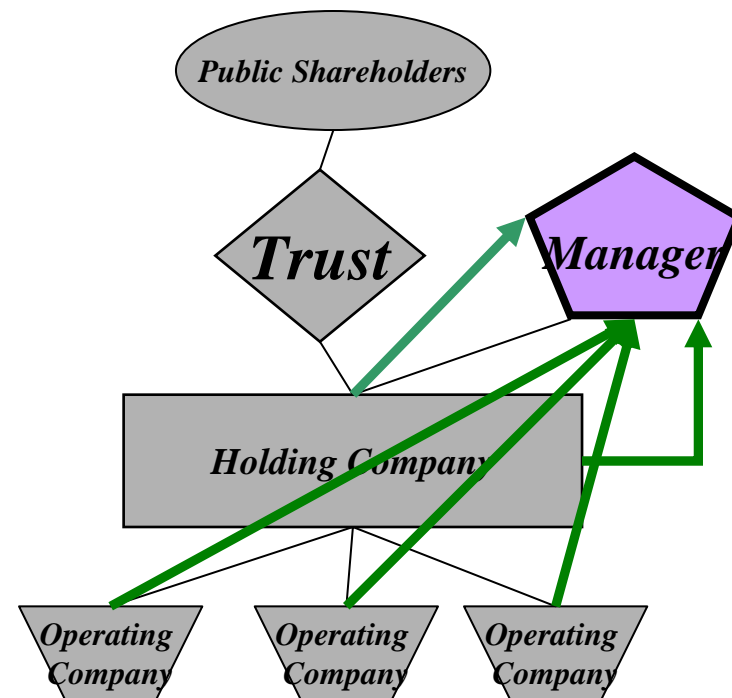
## Payments to the Manager

- The Manager may receive payments from the company or the operating businesses in the form of:
  - Management fees pursuant to management service agreement with the Holding Company.
  - Distributions from the Holding Company on the manager's class of equity securities in the Holding Company, if any.

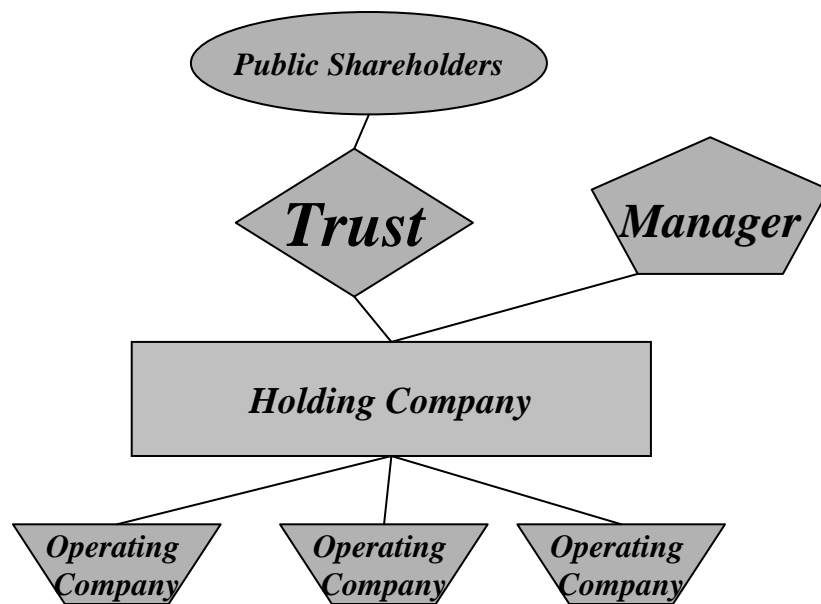


## Compensation of Manager

- The Manager may receive payments from the company or the operating businesses in the form of:
  - Management fees from management services agreements with the operating companies (likely offsetting, in part).
  - Transaction services fees from agreements with the operating companies for services beyond the scope of typical managerial duties.

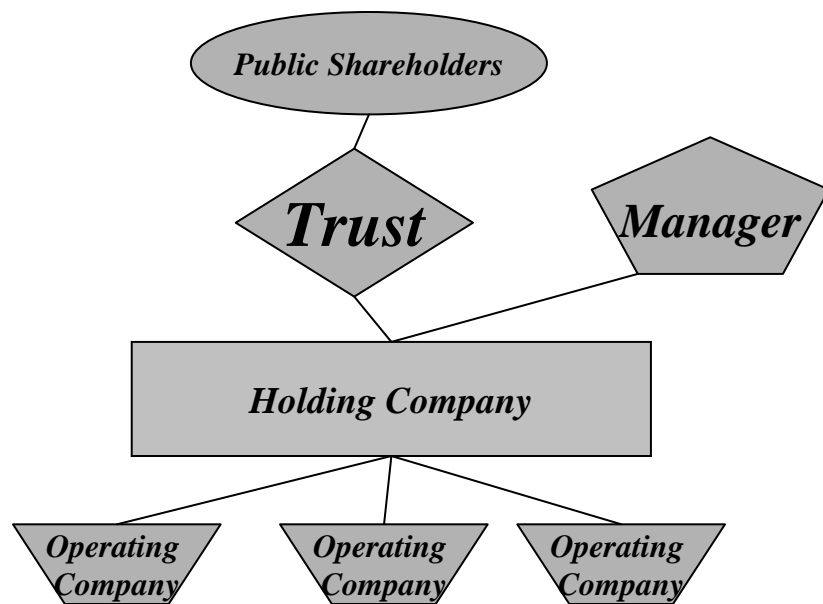


## Compliance Issues



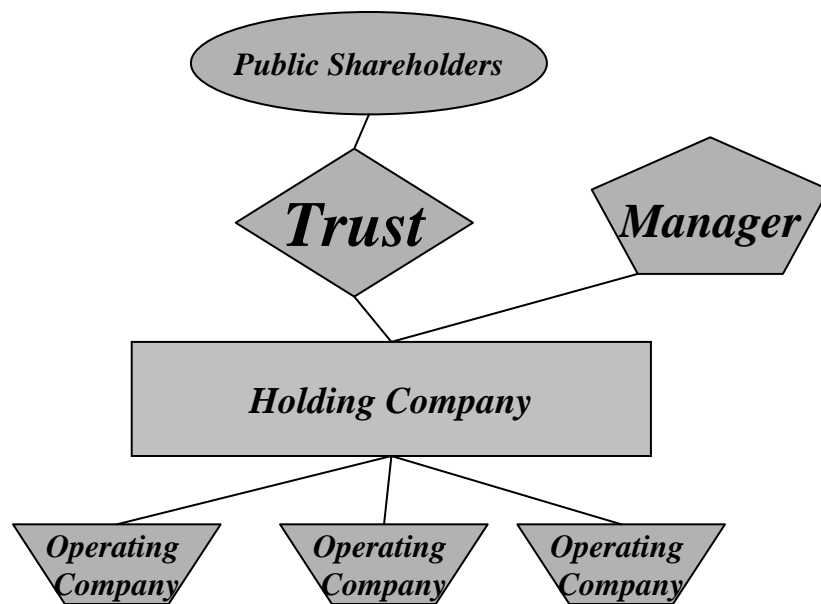
- Unlike BDCs, STACs may use consolidated financial statements in their annual and quarterly reports.
- Similar to BDCs, STACs have streamlined management structures.
  - External management. Manager pays the company's executive officers' compensation out of management fee. Simplified compensation disclosure.
- SOX Compliance –
  - Trust must comply with 404 requirements. However, Trust has no operations; must look to Holding Company and operating companies.

## Accessing the Market



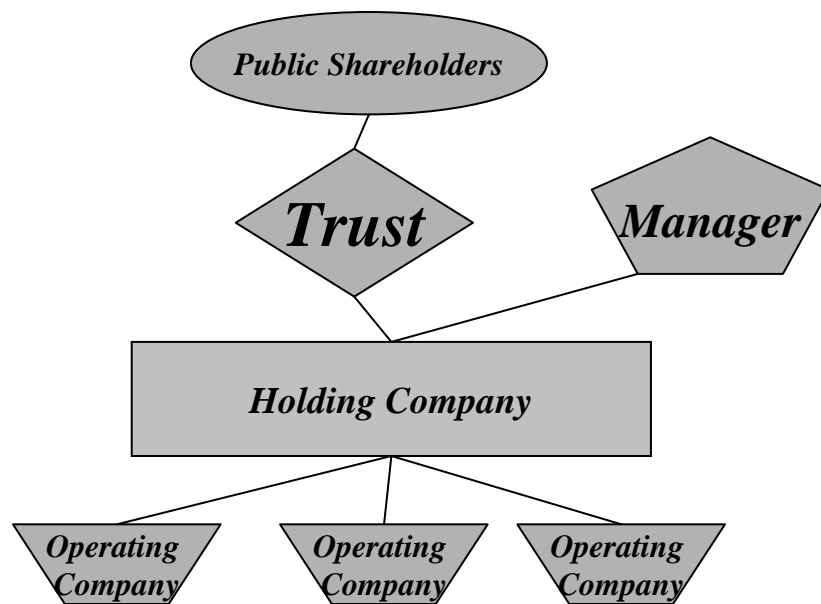
- STACs have been listed on NASDAQ and NYSE.
- Important factors to consider when listing include:
  - Collapsing trust structure;
  - Meeting exchange governance and compensation standards ; and
  - Whether to acquire operating companies concurrent with initial public offering.

## Accessing the Market



- Following their initial public offerings, the two existing STACs have successfully acquired and sold several operating companies.
- One STAC has recently announced a follow-on offering of 7,500,000 trust shares.

## Market Analysis



Without much operating and market history to draw upon, it is unclear the extent to which the STACs structure will gain widespread acceptance in the investment and financial communities. However, the STACs structure offers distinct benefits to investors and private equity managers who focus on making control investments over other vehicles. As a result, the STACs structure offers a unique perspective on the latest trend of using non-traditional means to take private equity public.

## What's next for STACs, SPACs and BDCs?

- Though the form is unclear, the continued growth and success of private equity will only provide greater incentive for private equity managers to tap into the public market.

Thank you for attending the STACs Webinar. For more information on Taking Private Equity Public, please visit our Web site at <http://www.publiclytradedprivateequity.com>. For more information on our presenters, please click below or visit Sutherland Asbill & Brennan LLP at <http://www.sablaw.com>:

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