Morgan Lewis

VENTURE CAPITAL & PRIVATE EQUITY FUNDS
DESKBOOK SERIES

Website: Friend or Foe?

Many venture capital firms and private equity firms create and maintain websites—usually eponymous—to achieve such far-ranging goals as building brand recognition, communicating with their existing investors, and creating channels of information with existing and potential portfolio companies. It is appropriate to use a website for such purposes and others, such as describing the industry sectors of interest to a venture capital or private equity firm, provided that certain precautions are taken as described in this article. Caution is warranted when establishing a website because there may be unintended legal consequences lurking within seemingly harmless web content. A scrubbed website can be a true friend for a venture capital or private equity firm. A neglected or carelessly composed website can be a terrible foe.

Do Not Solicit Investors

When engaged in a private offering (i.e., raising a fund), it is important that venture capital firms and private equity firms keep in mind that many of their funds are relying on exemptions to a number of different securities laws that all have one common requirement: there must be no public offering of securities by or on behalf of any of such private funds managed by such firms. Websites are generally viewed as being publicly available. Regulatory authorities, such as the Securities and Exchange Commission (SEC), have adopted very broad views of what constitutes an offering. As such, any materials on a website that could be viewed as a general solicitation or general advertisement may be considered a public offering by the SEC or other regulatory authorities.

To ensure compliance with the private placement regulations, and thus avoid an accidental public offering, it is best practice not to provide any fundraising information or materials over a website that is accessible by the public. Private placement memoranda, subscription agreements, investor questionnaires, and other materials typically provided to prospective investors should not be available on a firm's public website. Similarly, any data that could be viewed by the SEC or other regulatory authorities as designed to intrigue investors runs the risk of being viewed as an offer, such as naming specific venture capital or private equity funds managed by the firm or providing IRRs or other data showing the success of the firm's venture capital or private equity funds.

A good rule of thumb to steer clear of trouble is to focus the public portion of a website on the business of the firm, investing in portfolio companies. By focusing on the firm as a whole, no single fund is identified. By focusing on portfolio companies, you reduce the risk of the SEC or other regulatory authority taking the view that you are attempting to attract investors for your funds.

Use Password-Protected Website Areas

While the public portion of a firm's website should not be used to communicate with limited partners (as discussed above), one method of being able to use a website for effective communications with limited partners is to have an area of the website that is accessible only by password. In such a password-protected area, firms may post materials that might otherwise create concerns under the private placement regulations. Password-protected areas of a website are also useful for communicating

sensitive information to existing limited partners in the firm's funds. The passwords provided to users can also be used as a control mechanism to restrict the information any particular user has access to, as well as to monitor what information such user has, in fact, accessed. Many firms that used password-protected areas on websites often make such areas "read only." Do not rely too heavily on the effectiveness of "read only" technology. There are many countertechnologies that enable printing, saving, and distribution of purportedly "read only" websites. Another approach used is to design the password-protected areas of a website such that materials printed from such areas automatically have a watermark showing who printed the materials.

Do Not Hold Yourself Out as an Investment Adviser

Most venture capital and private equity firms do not operate as registered investment advisers. A critical requirement for exemption from being required to register is that such firms do not hold themselves out to the public as being investment advisers. As such, we recommend that firms do not describe themselves as investment advisers, money managers, or asset managers, or otherwise state that they provide investment advice. Even with respect to firms that are registered as investment advisers, because of the nature of the venture capital and private equity fund business, there is a fine line between holding yourself out to the public for your investment advisory services and making a public offering of limited partner interests in your funds. As such, we recommend that even registered investment advisers not describe their investment advisory services on their websites, although it is, of course, appropriate to state the mere fact that you are registered as an investment adviser.

General Partners vs. Managing Members vs. Managing Directors

Few, if any, individuals who run venture capital or private equity firms are general partners in the modern era of private investment funds. Most, if not all, venture capital funds and private equity funds have an entity as the general partner of the fund. The general partner entity is typically formed as a limited liability company. That entity is then owned, either directly or indirectly, by the people who call themselves "general partners" when, in fact, they are managing members of the limited liability company. The distinction is important because managing members of a limited liability company do not have general liability (i.e., they do not have personal liability for the obligations of the entity). General partners, however, have general liability (i.e., personal liability for the obligations of the entity). The risk of continuing to call yourself a general partner if you are not actually the general partner of the fund is that you may lead third parties to believe that you are, in fact, a general partner and thus responsible for the general liabilities of the fund. General partner liability is not limited.

We recommend that the principals of venture capital funds and private equity funds use titles such as "Managing Member" or "Managing Director" instead of "General Partner" to avoid general partner liability.

Disclaim All Obligations of Confidentiality

If a venture capital firm or private equity firm allows for electronic submissions of materials from potential portfolio companies, we recommend making it very clear that you do not have any responsibility to keep such information confidential. Similarly, it is important to have a "Terms of Use" page that requires the user to agree that none of the information being provided is proprietary. This may seem to be a hard position to take, but the fact is that venture capital firms receive numerous submissions, many of which are very similar. It is not appropriate for such firms to take on the risk that a potential portfolio company makes a claim that you inappropriately disclosed or misused any confidential or proprietary information.

Take Care Regarding Content, Regardless of the Source or Date

There are several areas in which venture capital firms and private equity firms may stumble into trouble as a result of the source or timeliness of the content of information on their websites.

First, to the extent third parties are able to post content, they should be subject to a "Terms of Use" page and clear disclaimers that the content was not provided or endorsed by the firm.

Second, to the extent professionals within the venture capital firm or private equity firm use any area of the website for blogs or similar informal styles of web-based communication, it should be understood by all that the courts do not distinguish between formal website content and informal blogs. All of the advice in this article applies to blogs and other informal web-based communications to the same extent as the formal areas of a website.

Third, it is important to task someone within a venture capital fund or private equity fund with the responsibility of keeping the website current. Old information can lead to problems, both legal and practical. Before updating a website, we recommend retaining records of what the website said. Keeping an ongoing file of everything your website has contained may be of great assistance in future legal proceedings.

Last, we recommend a general legal notice as follows: "The information on this website is intended solely for the benefit of firms and companies seeking private equity investment capital by providing general information on our services and philosophy. The material on this site is for informational purposes only and does not constitute an offer or solicitation to purchase any investment solutions or a recommendation to buy or sell a security nor is it to be construed as investment advice. Additionally, the material on this site does not constitute a representation that the solutions described therein are suitable or appropriate for any person."

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For more information on the issues discussed here, please contact your Morgan Lewis Private Investment Funds Practice attorney.

About Morgan Lewis's Private Investment Funds Practice
Morgan Lewis has one of the nation's largest private investment fund practices and is ranked as "#1 Most Active Law Firm" in the U.S. based on the number of funds worked on for general and limited partners by Dow Jones Private Equity Analyst (2011).

About Morgan, Lewis & Bockius LLP
Morgan Lewis provides comprehensive transactional, litigation, labor and employment, and intellectual property legal services to clients of all sizes—from global Fortune 100 companies to just-conceived startups—across all major industries. Our regulatory and industry-focused practices help clients craft and execute strategies to successfully address legal, government and policy challenges in today's rapidly changing economic and regulatory environment.

Founded in 1873, Morgan Lewis comprises more than 3,000 professionals—attorneys, patent agents, employee benefits advisors, regulatory scientists and other specialists—in 22 offices in the United States, Europe and Asia. The firm is unified in its longheld service philosophy that every action of our attorneys, in every representation, is driven first and foremost by the immediate and longterm concerns of each client. For more information about Morgan Lewis or its practices, please visit us online at www.morganlewis.com.