Why You Should Consider a "Permanent Capital" Investment Strategy

***Tom Blaisdell**, Executive Director, Center for Private Equity & Entrepreneurship (CPEE) at the Tuck School of Business at Dartmouth College*

Suppose you had a large pool of capital to invest for a very long time, perhaps "forever" in the case of an endowment, charitable foundation or even a Family Office or Sovereign Wealth Fund. How attractive would you find the following proposition: you can invest as much as you like in a Private Equity vehicle that will return over 20% compounded annual gain for the next 50 years with complete liquidity, marked to market every day the NYSE market is open. It will be highly tax efficient, with no dividends and no distributions (effectively an "infinite" reinvestment rate), so you only pay capital gain taxes when (*if*) you ever sell your position, allowing your investment to compound tax-free over the decades. And by the way, there is no "2 and 20" compensation scheme: the lead investment manager takes an annual salary of $100,000 while committing 99% of his net worth to being invested side-by-side with your investment on exactly the same terms.

Of course this is roughly the value proposition that Berkshire Hathaway has delivered over the last 50-plus years. With the benefit of hindsight, while a public company, Berkshire Hathaway and its legendary leader Warren Buffett have delivered an astonishing return record for what is essentially a "Private Equity" strategy. In essence, Buffett considers every investment, whether in public or private securities, as an "acquisition" of either a portion or the entirety of a company, so as a partial or full "purchase" of a "company", not as a "trade" in a "stock". Perhaps more importantly, Buffett takes a very long term approach to his investing strategy, famously stating "our favorite holding period is forever."[i] A commitment to provide "permanent capital" is one of Berkshire's core values that makes it an attractive acquirer and has arguably been a key driver of their impressive investment results.

This permanent capital strategy, while clearly not new, is both highly underutilized among entities with a reserve of permanent capital and also not unduly difficult to implement as a strategy, and certainly no more difficult (or costly) than the private equity strategies commonly employed by stewards of large capital pools.

If your organization has "permanent capital" (a base of capital that will not reasonably need to be spent or is prohibited from being spent in any currently anticipated timeframe) there are several reasons to consider an allocation to a permanent capital investment strategy within the Private Equity asset class. A permanent capital strategy has the potential to provide superior returns based on:

1. Better entry prices
2. Fewer transaction costs
3. Tax advantages, and
4. Better exit prices

A permanent capital strategy also has the potential to provide lower risk and better values alignment. We will discuss all these potential advantages in further detail below.

There are, of course, potential costs, disadvantages and risks associated with a permanent capital strategy as well. These include the obvious, such as illiquidity, but also the less obvious, such as misalignment of interests in various structures that might be employed, and incenting company management and investment management teams. Many of these disadvantages and challenges can be addressed with mundane though potentially complicated tactics, and should not prevent one from considering the potential advantages of pursuing a permanent capital strategy.

Before we explore the rationale for a permanent capital strategy further, we should spend a moment describing the strategy in more detail, including who it might be appropriate for and examples of the strategy currently in practice.

Who Has Permanent Capital?

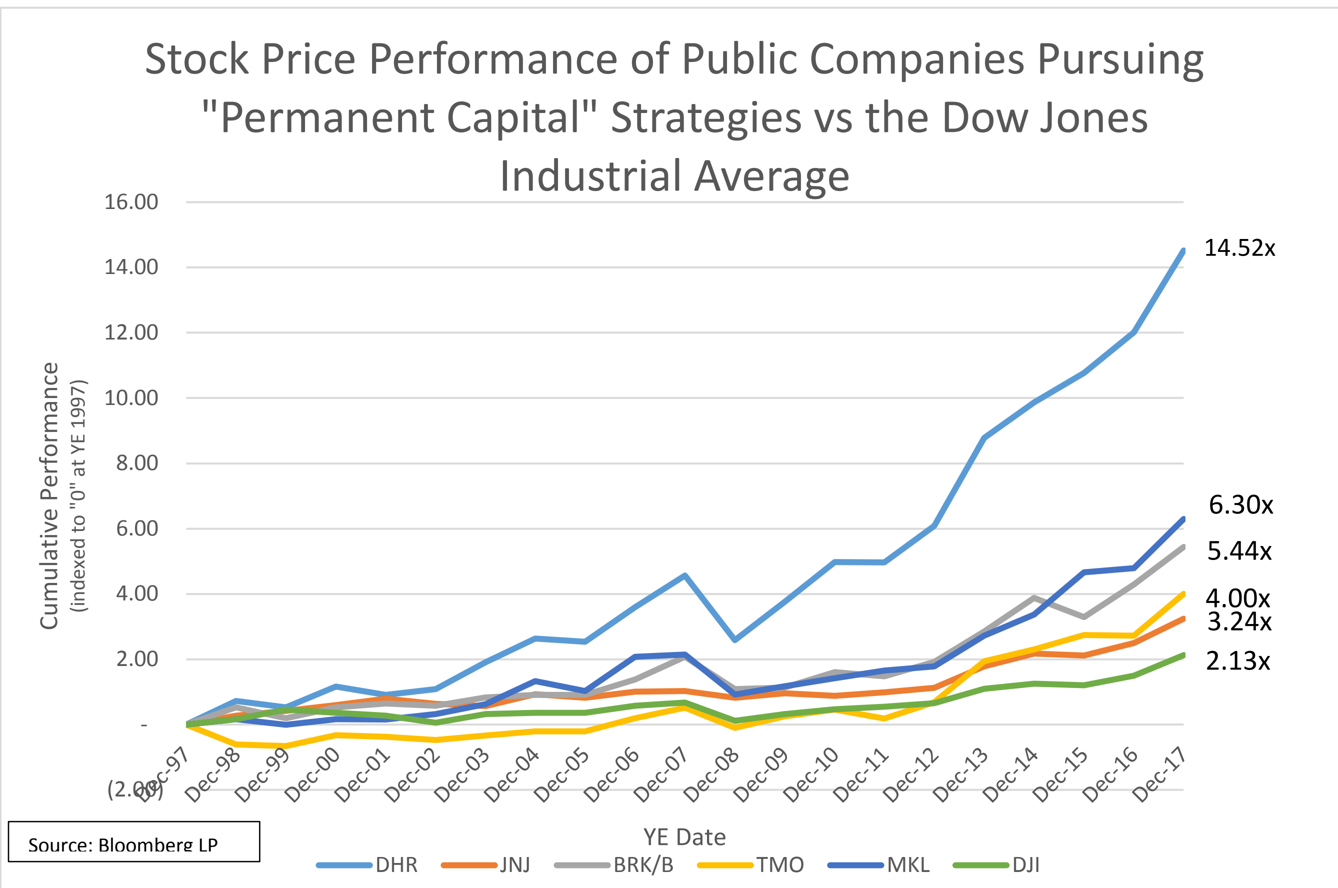
As mentioned above, permanent capital can be defined as "capital that will not reasonably need to be spent or is prohibited from being spent in any currently anticipated timeframe." Organizations such as endowments, foundations, family offices, insurance companies, pension plans and Sovereign Wealth Funds (SWFs) all will typically have significant holdings of permanent capital. Indeed, any organization with substantial investment assets might consider some percentage of their asset base to be "permanent" on a probabilistic basis, in that at any given time there is a certain percentage of their assets that they have no reasonable expectation of having to access/spend in any current or anticipated planning horizon.

Examples of Investors Employing Permanent Capital Strategies.

Permanent capital strategies are not new. In fact one could argue it is one of the oldest strategies around, as for centuries assets in families have often been concentrated in "permanent" vehicles such as family businesses, land holdings, etc. But in contemporary investment management practice, with its focus on year-long performance periods as benchmarks, much less attention and discussion is given to permanent capital strategies than other more active or even passive, index-oriented portfolio construction strategies. That said, it is helpful to identify some of the high profile and not-so-high profile investment managers employing a permanent capital strategy as they will provide many of the illustrations of the potential benefits and limitations of this strategy.

Perhaps the most recognizable example of an organization pursuing a permanent capital strategy is Berkshire Hathaway, led by its folksy yet charismatic founder and CEO Warren Buffett. A simple example of Berkshire's "permanent capital" approach to buying businesses is its purchase and long-term ownership of See's Candy. When Berkshire bought See's Candy they saw it as a fundamentally attractive business that would continue to grow and generate profits over a very extended timeframe ("forever"); they did *not* make the investment with the intention of "flipping" the company to another buyer—strategic or financial—in a 3 to 5 year timeframe typical for most private equity firms.

While Berkshire Hathaway may be the most visible company/investor pursuing this strategy, there are many others. Public companies pursuing similar strategies of buying and holding entire companies, in related industries or not, include Markel Corporation (MKL), Danaher (DHR), ThermoFisher (TMO) and Johnson & Johnson (JNJ). In the case of JNJ, one could argue that they are in essence a “sector-focused” Berkshire Hathaway in the life sciences and pharmaceuticals space. They buy entire companies in these sectors with no intention or plan to “flip” them for a profit, but keep them separate and independently run (JNJ has over 250 subsidiaries). Comparing the returns on the stocks of these companies versus the Dow Jones Industrial Average over an extended 20 year period shows strong outperformance versus the average by all of them. While this is not conclusive data that a permanent capital strategy outperforms an industry average, it is anecdotal evidence—an “existence” proof if you will – that investors (or companies) can and do pursue permanent capital strategies, at scale, with superior results to an industry average.



Examples are a bit more difficult to document in the private equity world, but a number of funds and firms employ more long-term oriented structures that allow the investment managers to pursue more permanent capital strategies. Some illustrations include the decades old evergreen structure of Sutter Hill Ventures' fund on the venture capital end of the spectrum, up to Blackstone's more recent offerings of a longer duration 20 year private equity fund[ii] and an "open-ended" real estate fund, Blackstone Core Plus Real Estate Partners, which does not have a fixed end date. Blackstone's president Tony James commented "We love to hold our winners" and "…we see [Blackstone] moving more and more towards permanent capital vehicles."[iii] And of course family offices, large pension plans and sovereign wealth funds have been employing permanent capital strategies for as long as they have been around, owning businesses and real estate with unlimited holding periods.

POTENTIAL ADVANTAGES OF A PERMANENT CAPITAL STRATEGY

As outlined above, there are many potential advantages of a permanent capital strategy versus the strategies typically employed by Private Equity (PE) funds. For comparison purposes, a typical PE firm might normally state their investment strategy as targeting "3x to 5x in 3 to 5 years", meaning they are hoping to make 300% to 500% return on their original investment by holding a company for 3 to 5 years and then selling it, perhaps collecting dividends along the way. (For convenience, we will refer to this as a "3 to 5" strategy) All of the advantages below should be considered "relative" to a "3 to 5" strategy, so whatever baseline returns you consider might be achievable with a "3 to 5" strategy, the advantages below would accrue to an outperformance above those returns. The point of this argument is to be "directionally correct", i.e., that these really are advantages and not just neutral or even disadvantages relative to a "3 to 5" strategy.

Better Entry Price

In many cases when a company is being sold (or is selling significant equity in the business), the sellers are simply looking for the best economic deal they can get. In some cases, however, non-economic considerations can play a major role as well. These considerations may include the ability for the sellers to continue to participate in the business going forward; job protection for management as well as rank and file employees, or to a community being served; and even a commitment to ongoing preservation of the 'values' of the company being sold.

Many company founders are committed to building "legacy businesses", with no interest in taking the company public or continually "flipping" the company from one financial sponsor to the next (the natural paths of a "3 to 5" strategy). Typical PE investors often talk about "having the exit in mind when the deal is made," but these founders/owners don't have an exit on their mind at all. They founded their businesses to serve a customer, not just to make a profit, and their vision is to serve more customers, better, every year, and yes, over time, to build a valuable asset for their families and employees. Ideally these founders/owners would find like-minded "permanent capital" providers that are interested in growing value in and through the business rather than by trading the business from one owner or investor to the next. And in many cases, they are willing to take a lower price for their business (or shares in their business) to guarantee they can continue to operate their business in this manner.

The history of Berkshire Hathaway includes many examples of acquisitions and investments where Berkshire was able to obtain a better price for a business based on its promise of "permanent capital." One specific example with actual numbers revealed is the case of Berkshire's purchase of RC Willey in 1995 for $175 million based on the alignment of cultures, even though the family had received offers greater than $200 million for the company.[iv]

Fewer transaction costs

Every time a company is sold and bought there are substantial transaction costs—"frictional losses"—that are dilutive to the company and/or its owners. These expenses include legal fees, banker fees, accounting fees, consulting fees, and of course the immeasurable distraction costs of the transaction. These fees can easily run to 5% of the value of the company and even higher at each transaction point. Considering a 30 year time horizon for a company (long, but not forever) and the usual time horizon of a typical private equity owner of five to seven years (generously, as their target is usually three to five years), this would imply four to five transactions over the 30 year horizon times the associated drag of transaction costs on each transaction. Compare this to having continuous ownership by one entity through the 30 year period and the potential for saving and reinvesting these transaction costs appears self-evident.

Differential transaction costs also show up in the investment management costs generated by the different strategies. By definition, a permanent capital strategy yields a lower portfolio turnover rate than a typical private equity fund. Private equity investment managers perform several functions over the life of a fund: they source, diligence, and select investments; drive value-improvement projects and initiatives within the companies they invest in; then take the company through an extensive sales process (either an IPO or M&A process) to maximize their value in an exit. And then they do it all over again, and again.

By buying and holding companies rather than buying and selling companies and then buying some more, investment managers executing a permanent capital strategy will indeed have to do the upfront sourcing, diligencing, and selecting of investments. But then they may or may not invest a great deal of effort in value improvement projects, depending on whether their strategy is to buy great companies at fair prices and leave them alone, or buy fixer-uppers that they improve to the point of being strong, stable companies not requiring ongoing intervention from the investors.

And at this point, the strategies (and costs) diverge significantly. Rarely will effort be expended or costs incurred selling a portfolio company, and for a given amount of capital employed against the strategy, far fewer companies will have to be sourced, diligenced, selected and potentially fixed.

For illustrative purposes, let's assume an investor wants to deploy $500mm in a private equity strategy. In a greatly simplified example, with a traditional strategy, let's assume a five year average hold period and ten $50mm investments in the $500mm fund. To keep the $500mm fully invested (again, simplifying greatly), the firm would have to make ten investments every five years. The traditional firm would need to buy and sell 60 companies over the same 30 year period assumed above, while the permanent capital strategy investors could invest and hold 10 companies over the same 30 year period. Clearly the traditional approach creates a lot more work sourcing, diligencing, selecting, fixing and selling companies that the permanent capital approach, and would require far more (and expensive) investment managers to implement it. The traditional approach—with its 120 transactions (60 companies bought and sold) versus 20 transactions (10 companies bought and sold) for the permanent capital strategy—would also make a lot of bankers, lawyers, consultants and accountants very happy!

On a side note, one other activity that investment managers perform is fundraising, which creates substantial costs of its own in terms of expense, time and distraction. While it's true that structures to support permanent capital strategies may be more complex and expensive to set up initially, if done properly they can radically reduce or even eliminate fundraising costs over time. For the traditional firm in the example given above, it is likely they would have had to take time, effort, distraction and expense to fundraise seven to ten times during the thirty year period. A properly designed permanent capital structure would have a fraction of the fundraising costs associated with a traditional fund structure.

Tax Advantages

The potential tax advantages of a permanent capital strategy follow mostly along the same vein as reduced transaction costs, as with each transaction, assuming a gain by the seller, taxes would need to be paid on the increase in value. Moreover, if the company is sold multiple times over say a 30 year period, sometimes for a gain, sometimes for a loss, the gains and losses would accrue to different parties who would not be able to net them out against each other. Even on a holistic basis, assuming that in aggregate PE firms as a whole provide positive returns over time, the more transactions that occur, on a net basis, the more taxes that will be paid <u>prematurely</u> due to realizing gains on a weighted average basis earlier than in a permanent capital strategy. The concept that taxes represent a real drag on investment performance is elementary: if you take your gains each year and reinvest them anew you don't just lose the dollars paid in tax each year, but also the lost compounding of those dollars over future years.

An extreme example of this can again be seen by looking at the case of Berkshire Hathaway. On an individual level, an analysis done by Barron's Magazine in April of 2015 calculated that in 2014 alone, by holding his position in Berkshire, which adheres to a policy of zero dividends and reinvesting its capital internally rather than paying out dividends at the average rate of the S&P 500, Warren Buffett personally "avoided" dividend income of about $1.2B and a tax liability that year of $280MM.[v] That is $280MM that continues to be at work generating future earnings for Buffett rather than going to the US Treasury for as many years as he chooses to retain his holdings of Berkshire. It is not an overstatement to say that Buffett has billions of dollars working for him solely as a result of the "buy and hold" and the internal reinvestment strategy of Berkshire Hathaway.

Of course the same principal applies to anyone who invests in a company that simply reinvests in the company's business and grows retained earnings rather than generating dividends, and importantly doesn't sell the company generating "unavoidable" capital gains to the owners/investors. While difficult to capture in hard numbers, it seems plausible that deferral of taxes is one of the biggest transaction cost savings of a permanent capital strategy versus a "3 to 5" trade-out strategy. While less important to non-taxed entities such as certain endowments and foundations, any entity subject to substantial tax rates should explicitly factor in the tax drag of the "trading" approach of traditional PE firms versus the "buy and hold" approach of a permanent capital strategy.

Better Exit Price

Nothing lasts forever.   While we refer to the strategies in this paper as "permanent", that is actually shorthand for "having a very long time horizon with no pressure to sell." A truism in the private equity business is that "it's always better to be bought than sold." But as a fund approaches (and often overshoots) its fund life, many firms are in exactly the position of having to sell a portfolio rather than waiting to be bought, and anyone who has been in that situation knows exactly how uncomfortable a position it is.

On the other hand, if a company is profitable and growing and has no intention of selling itself in the foreseeable future, it is likely over time that it may be approached by interested buyers. If the company decides to sell in this situation, it will be on its own terms and timing, which may be very advantageous indeed. It is difficult to produce data in a rigorously analyzed way that supports this advantage, but from a purely logical and intuitive point of view, it seems like an eminently rational assumption to accept.

Lower Risk

Risk in investing is often measured as volatility, or beta. But if one expands the concept of risk to the broader context of "failing to meet one's goals," a number of other dimensions or components of risk come in to play. Two other primary risks would be the risk of failure (including bankruptcy or other loss of all equity value) and the risk of underperformance (both on a short term and long term basis). One must also consider that these risks are not necessarily symmetric between the investors and founders/management, so to the extent that reputational risk is also important, ensuring alignment on matters of risk between the two groups is also critical.

Risk as measured by volatility alone addresses the possibility that you might have to sell an asset when its price is at an ebb value. If an investor not only doesn't have a need, but not even an intention to sell in any given timeframe, as with a permanent capital strategy, this type of risk would be *de facto* lower than that for an investor working within the context of a fixed fund life/timeline.

The risk of failure of the business (including bankruptcy or other loss of all equity value) contains perhaps the greatest risk of misalignment of interests between investors and founders/management. Investors will have diversified portfolios, greatly diminishing the risk presented by the failure of a single portfolio company, whereas founders/management will be much more exposed to both material financial risk as well as reputational risk arising from the failure, or loss of control, of their company.

One way this risk profile difference might manifest itself is in the use of leverage. Typical PE investors will often increase debt loads on acquired companies (beyond what was previously carried and also beyond what might be employed if the company were simply being managed as a "going concern") and sometimes will "recap" the balance sheet (add debt and payout dividends to equity owners) several times during their ownership period. These periods of heightened debt load could also be considered a *de facto* indication of higher risk for a company, with perhaps small, but still material, increases in the risk of business failure. (Just ask the managers and employees of some of the recent retailer LBOs.)

Private equity managers would argue conversely that the companies they acquire are at risk of underperformance, especially in terms of Return on Equity (ROE), by being too cautious in their use of leverage. While that may be true within a given time period, the question remains as to whether it increases the risk to the company itself. Again it seems a truism that more debt is more risky from a potential business failure perspective than less debt, and therefore the risk to the company's existence is *de facto* greater with a higher level of debt. There may be a higher return on equity at any given point in time to compensate for that risk, but it is hard to argue there isn't greater risk, and more to the point that the risk of failure is a materially different kind of risk from the risk of short term underperformance, especially from the point of view of founders, managers and employees.

There is also another side to the story of underperformance risk as well. Private equity owners will often shorten their decision making horizon as the time nears for them to begin exiting their position. Knowing that a great deal of the value they will realize in a sale will be based on the EBITDA (or other cash flow metric) a company generates in the two years before a sale, decision making will be skewed to short term profitability over long term strategic investments. In street parlance, this is sometimes referred to as "putting lipstick on the pig" or "dressing it up for sale." The risk here is less that the company might go bankrupt and more that it will underinvest in NPV-positive investments that would strengthen its long term profit-generating potential, thereby boosting short term performance, but leading to long term underperformance.

The interests of long-term oriented founders/managers could be better aligned with investors employing a permanent capital strategy in terms of both risk of failure and the risk of long term underperformance of a business.

Values Alignment

A big, but admittedly more qualitative, potential advantage of a permanent capital strategy is the ability to create values alignment within a concentrated portfolio. Many family offices, endowments and even pension funds and sovereign wealth funds already try to implement some level of "values-based", SRI (Socially Responsible Investing) or ESG (Environmental, Social and Governance) approaches to investing. At a minimum, they often try to avoid contentious investments in areas such as alcohol, tobacco, gambling and pornography, which are difficult to avoid in blind pools and passive index funds.

Building a concentrated portfolio of companies with zero to very low company turnover means that an investing platform can wait until target companies match their values as well as their investment objectives. As in our previous example, finding 10 great companies that are consistent with an investor's values is easier than finding sixty.

As their titles suggest, two recent books, *Berkshire Beyond Buffett: The Value of Values* and *Conscious Business: How to Build Value Through Values*, both explore the concept of building value through focusing on values. A permanent capital strategy, with its low portfolio turnover, has the luxury of focusing more explicitly on values as one of their investment selection filters.

POTENTIAL CHALLENGES OF A PERMANENT CAPITAL STRATEGY

There are several important challenges associated with permanent capital strategies, and it should be noted that permanent capital is certainly not the best capital strategy for every investment situation. Challenges can be grouped into the following categories:

1. Lack of Urgency/Bias Towards Action
2. Managing Liquidity
3. Incenting/Compensating Investment Managers
4. Aligning Interests Among Permanent and Non-Permanent Capital Providers
5. Structuring Investment Vehicles for Permanent Capital Strategies

Most of these categories are actually overlapping (e.g. lack of liquidity creates challenges in incenting investment managers), and many of them can be addressed at least partially by following best practices related to the last set of challenges around structuring investment vehicles for implementing permanent capital strategies. We will raise the primary issues in each set of challenges briefly, but not try to solve all cases in this paper. Suffice it to say there are ways to address each set of challenges that are being used in practice every day, but the real questions are: at what cost, and is the cure more expensive or damaging than the disease?

Lack of urgency/bias towards action

One of the first rationales a typical PE manager will give for having a pre-specified time horizon for an investment is the sense of urgency that it instills in an organization. The PE buyer comes in to each deal with conviction around a plan of action to create incremental value over a specified period of time, and this creates a sense of urgency and an alignment of priorities that drives incremental value creation that would not have occurred under "business as usual." They also argue that they can bring a stronger sense of rigor and accountability to entrenched and lazy management teams, oftentimes with extensive changes to the management team itself. While this is certainly the case in many private equity investment situations and is one of the primary ways PE firms create value, it is by no means an argument against permanent capital.

In both cases, this argument presupposes that current management is not doing the most effective job it could be in creating value in the company. Many permanent capital investors would argue you should not be acquiring "broken companies" in the first place. Warren Buffett has discussed his conversion from buying "fair companies at a great price" to buying "great companies at a fair price."[vi] This would include targeting companies with strong management teams that already focus on getting the most out of every investment dollar in a company. Buffett states: "The really good manager does not wake up in the morning and say, 'This is the day that I am going to cut costs,' any more than he wakes up and decides to practice breathing."[vii]

But there is a good argument to be made for a strategy of buying "broken companies" and fixing them, and then selling them down the line, flipping companies like flipping houses. An interesting question then is, if you just fixed the company and it is now a "good" company, why not continue to own it? Or is it only good for a short shelf life, and you have to flip it before it becomes a non-performer again? Perhaps the PE partner argues that the company now needs to do an IPO or be bought by a "strategic" buyer in order to get to the next level. Fair enough. But there is data to indicate that in a majority of cases, the target company is sold by one PE firm and bought by another[viii], with the acquiring PE firm presumably having "conviction around a plan of action to create incremental value." Was a transaction, with all the concomitant transactional expenses, really required to unlock all that additional incremental value?

There are certainly many instances where PE firms can add significant value by coming in to underperforming, poorly capitalized or ineffectively managed companies, and this essay doesn't in any way mean to argue that such a strategy isn't often effective. But the argument that having a shorter term perspective of a time-limited fund is necessary to create a sense of urgency or a bias towards action is not supported. Clearly some excellent management teams can and do act with a consistent sense of urgency and bias towards action even in non-PE owned companies, and an investor interested in applying a permanent capital PE strategy can either choose to pay a "fair price for a great company" with such a management team already in place, or alternatively buy a "broken" company, fix it, and then hold it as it grows value as a "great" company. Acting as a catalyst for change, a cornerstone of traditional private equity investing, is not contraindicated in a permanent capital strategy.

Managing Liquidity

The issue of liquidity is an interesting one. Ostensibly, by definition, liquidity for capital allocated to a permanent capital strategy shouldn't be a concern: the capital is meant to be permanently invested, so there is no need for liquidity. And yet as we have described previously, "permanent" is really just shorthand for "a very long time," and for a variety of reasons (estate planning for family offices, strategy changes for pension plans, "Black Swan" events for insurance companies, etc.), practically speaking, liquidity issues will need to be dealt with in some manner. Options for providing liquidity will be determined primarily by the legal structure chosen to implement a specific permanent capital strategy, and any investor or set of investors will need to choose the optimal structure for the potential liquidity needs and timeframes for their situation.

Incenting/Compensating Investment Managers

Liquidity issues in permanent capital structures pose a special problem for compensating the investment managers implementing the strategy. Typically PE investment managers are compensated primarily in two ways: fees and "carry." Fees are meant to pay for startup costs and on-going management of the fund, including salaries for the investment professionals, and "carry" is meant to provide the "upside incentive" and "alignment of interests" similar to the way stock options or Restricted Stock Units (RSUs) are used in operating companies. The "carry" is where the difficulty arises in permanent capital strategies. Carry is normally paid out over the life of the fund as "realizations" or exits are made from portfolio company investments. This is already a long-term proposition for PE investment managers, as typical portfolio company holding periods can easily span three to seven years and longer, and funds span at least a decade. In many cases investment managers also have performance hurdles that must be cleared before carry can be earned or distributed, further extending the time before this compensation is realized.

It becomes quickly apparent that a permanent capital strategy only compounds this challenge. If companies are not sold but held indefinitely, when does the investment manager "earn" his or her carry? When does it get paid out? This is a thorny issue and one that needs to be addressed either with added complexity to the structure of the investment vehicle or through selection of investment managers that are willing to have the "performance" portion of their compensation be provided through ownership of the permanent capital vehicle itself or most likely a combination of both.

Aligning Interests Among Permanent and Non-Permanent Capital Providers

Most private equity investors take control positions in the companies they invest in, the better to drive the changes they envision as necessary as well as to control the planned eventual exit. In some cases, some private equity investors will make minority investments, usually when they are co-investing with other PE investors they know to be like-minded in terms of operations and time horizon or when they have protective provisions that essentially give them control of important aspects of the company governance (such as when to sell) even though they don't own a majority of the equity.

Investors employing a permanent capital strategy have to take care in making minority investments without control provisions to ensure they have an alignment of interests with the other investors and owners around the table, who may desire liquidity on a faster timetable than they do. It would be a safer approach to focus on control investments, and at a minimum it would be good to have no "drag along" provision that could force them to sell, as well as a "Right of First Refusal" (ROFR) clause in the agreement with other investors around the table that allows them a first option to buy out the other investors if those investors wish to sell their shares.

Structuring Investment Vehicles for Permanent Capital Strategies

Choosing a structure for pursuing a permanent capital strategy requires the balancing of several considerations: taxation, liquidity, expense/administrative overhead, and manager/investor alignment. Several types of "typical" investment structures can be used in implementing a permanent capital strategy, but usually some level of modification is required to adapt. Structures to consider include:

- Deal-by-deal Special Purpose Vehicles (SPVs)
- Single Limited Partner Evergreen Funds
- Multiple Limited Partner Evergreen Funds
- C Corporations (public or private)

Each structure comes with its own tradeoffs regarding the considerations laid out above, and a more thorough review of these options and tradeoffs need to be considered before selecting and implementing a structure. Regardless of chosen structure, there are a myriad of decisions to be made within each structure, and these decisions also require more extensive investigation. The important thing to remember is that each of these approaches is already being used in practice to implement permanent capital strategies, so there is no need to "reinvent the wheel." Rather once you have decided to pursue a permanent capital strategy, just be sure to connect with a law firm with deep experience with each of the structures enumerated above specifically as applied to permanent capital strategies and work with them to choose and implement the best option for your particular situation.[ix]

CONCLUSION

For those organizations with stewardship of significant amounts of "permanent capital", there are several strong arguments to be made for employing a permanent capital investing strategy. Better entry prices, fewer transaction costs, tax avoidance and deferral, higher exit prices, potentially lower risk, and clearer values alignment are all potential advantages that could equate to measurably higher returns from employing such a strategy versus a typical "3x to 5x in 3 to 5 years" private equity strategy. This strategy is not new and there is much anecdotal evidence to support many of these arguments, and it would be valuable to pursue further research, both academic and practitioner-based, to better understand the underlying mechanics and better quantify the pros and cons of this approach to investing. But in the meantime, investment managers with large private equity programs may want to start experimenting with various permanent capital strategies to begin collecting experience with and enjoying the advantages of these approaches.

---

[i] Berkshire Hathaway Inc, 1988 Chairman's Letter, dated Feb. 28, 1989, http://www.berkshirehathaway.com/letters/1988.html, accessed Dec. 11th, 2017.

[ii] Louch, William. "Blackstone Collects $5bn for First Longer-Life Fund." Financial News, Financial News, 17 Mar. 2017, www.fnlondon.com/articles/blackstone-collects-5bn-for-maiden-longer-life-fund-20170317, accessed Dec. 11th, 2017.

[iii] Putzier, Konrad. "Blackstone Making Bets on Permanent Investment Funds." *The Real Deal New York*, The Real Deal New York, 2 Jan. 2018, www.therealdeal.com/2017/07/20/blackstone-bets-on-permanent-investment-funds/, accessed Jan. 8th, 2018.

[iv] Weverbergh, Raf. "Listen to Warren Buffett: Your Reputation Is Worth Cold, Hard Cash." *Entrepreneur*, Entrepreneur Media, 29 June 2016, www.entrepreneur.com/article/277160, accessed Jan. 8th, 2018.

[v] Propp, Morris. "Warren Buffett's Nifty Tax Loophole." *Barrons*, Barrons, 11 Apr. 2015, www.barrons.com/articles/warren-buffetts-nifty-tax-loophole-1428726092, accessed Jan. 9th, 2018.

[vi] Berkshire Hathaway Inc, 1989 Chairman's Letter dated March 2nd, 1990, www.berkshirehathaway.com/letters/1989.html, accessed Jan. 9th, 2018

[vii] Loomis, Carol. "The Inside Story of Warren Buffett." *Fortune Website* , Fortune, 11 Apr. 1988, archive.fortune.com/magazines/fortune/fortune_archive/1988/04/11/70414/index.htm, accessed Jan. 9th, 2018.

[viii] An analysis of exit events of PE portfolio companies from January 1st 2011 to December 31st 2016 in the Zephyr database, published by Bureau van Dijk, listed 38 IPOs, 306 sales to Strategic Buyers, and 1,049 sales to Financial Sponsors. Zephyr, published by Bureau van Dijk, queried on Jan. 10th, 2018.

[ix] For a good introductory overview of structures for Permanent Capital strategies, see "Permanent Capital: The Essentials" by Julia D. Corelli and Stephanie Pindyck Costantino (http://www.pepperlaw.com/publications/permanent-capital-the-essentials-2017-03-30/)