CLIENT MEMORANDUM

ILPA Proposes Template for Reporting of Private Equity Fees and Expenses

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With the backdrop of significant regulatory focus on private equity fees and expenses, the Institutional Limited Partners Association (ILPA) on October 22, 2015 released its proposed Fee Reporting Template for private equity firms.[1] The template calls for disclosure of a range of items, including fees and expenses that have been the subject of recent SEC enforcement activity.[2]

The ILPA is comprised of over 300 member organizations globally and represents over $1 trillion in private assets under management. ILPA in the past has published its Private Equity Principles as well as standardized reporting templates and best practices for capital calls/distribution notices and quarterly reporting generally. While ILPA has previously indicated that it was not the intent to require reports in the exact format of those templates, the FAQs accompanying the proposed Fee Reporting Template state that all managers are expected to provide this information to investors but that ILPA understands it may take time for managers to adapt their reporting platform to meet these expectations.

1 See For Consultation: ILPA Fee Reporting Template, available here

2 See Willkie Farr & Gallagher LLP Client Memorandum, "SEC Enforcement Action Related to Private Equity Fees and Expenses" (Oct. 8, 2015), available here and Willkie Farr & Gallagher LLP Client Memorandum, "Private Equity – Broken Deal Expenses" (July 2, 2015), available here

The proposed Fee Reporting Template itemizes Advisory Fees, Broken Deal Fees, Transaction and Deal Fees, Directors Fees, Monitoring Fees, Organizational Costs, Placement Fees and Capital Markets Fees. While many of these fees are now offset and reduce management fees paid by investors, at levels ranging from 50% up to 100%, institutional investors have indicated that it is difficult to trace the net fees paid across their portfolios. The template provides for reporting of management fees gross and net of offsets, waivers and rebates, for the quarterly period, the trailing 12 months and since inception.

The proposed template also specifies the amount of incentive compensation a general partner has received during the quarterly period, the trailing 12 months and since inception. In addition, the template discloses the change in accrued incentive compensation that would be paid to the general partner upon realization of all remaining investments in a fund at their current carrying value (which will need to be viewed in the context of the private equity J-curve, investment cycles and the long-term nature of private equity funds).

ILPA's previous reporting templates have provided guidance to private equity firms on expected levels of detail and disclosure, but have also met with resistance and been viewed as attempts to standardize a format for reporting that does not work for all managers or investment strategies. With respect to fees and expenses, it may be difficult to capture the varying nuances of fund agreements in a standardized form. In addition, providing more detailed information has been a concern for some managers due to state freedom-of-information act laws, when financial reporting is already provided in accordance with GAAP in a format that may lend itself to greater protections under the state FOIA statutes.

It remains to be seen whether efforts to standardize reporting of fees and expenses will be broadly accepted by private equity firms. Some institutional investors are insisting that managers adopt the ILPA template or comparable disclosure formats. In addition, some managers may view complying with the ILPA template on a voluntary basis as a better alternative than the developing legislative efforts that could require standardized fee and expense disclosure.[3] And the continuing enforcement focus on private equity fees and expenses could cause some managers to accept a more detailed, standardized industry disclosure format, with a view towards what may be emerging industry practices.

Private equity firms have an opportunity to comment on the proposed Fee Reporting Template by December 11, 2015. The template is expected to be finalized by January 29, 2016.

3 See the October 12, 2015 letter to CalPERS and CalSTRS from John Chiang, Treasurer of the State of California, calling for a state law, in the absence of federal rules, requiring disclosure of private equity fees and expenses charged to California public pension funds, available here and the July 21, 2015 letter to SEC Chair Mary Jo White, from a coalition of state and city treasurers and comptrollers, calling for new SEC rules requiring greater transparency regarding private equity fee and expense disclosure, available here

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