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ILPA Releases ILPA Principles 3.0

On June 27, 2019, the Institutional Limited Partners Association (ILPA) announced the release of "ILPA Principles 3.0: Fostering Transparency, Governance and Alignment of Interests for General and Limited Partners" (ILPA 3.0). ILPA 3.0 is available here.

Responding to what ILPA perceives to be a general partner-friendly market[1], ILPA 3.0 reasserts ILPA's focus on three guiding principles for effective private equity partnerships – alignment of interest, governance and transparency – and expands on guidance and best practices set forth in prior versions of the ILPA Principles (released in 2009 and 2011, respectively) and other previously published ILPA standards and guidance.

Although all of ILPA 3.0 deserves careful attention from both limited partners (LPs) and general partners (GPs), several topics stand out:

- Continued emphasis on fiduciary duties of GPs to LPs, which is noteworthy in light of recent interpretive guidance from the U.S. Securities and Exchange Commission (SEC) regarding the fiduciary duty of investment advisers. Note that ILPA believes that gross negligence, fraud and willful misconduct and breach of the Limited Partnership Agreement represent a minimum standard for carve-outs to the exculpation and indemnification rights of GPs under Limited Partnership Agreements.

- Detailed guidance on limited partner advisory committee best practices, which may be helpful to many GPs, in particular those forming their first institutional funds.

- Recommendations on the use of subscription credit facilities. Note that ILPA suggests that, where capital is drawn from a subscription credit facility collateralized by uncalled LP capital commitments, the LPs' preferred return should be calculated from the date on which the facility is drawn, rather than the date on which the capital is ultimately called from the LPs. ILPA believes that this approach better aligns the LP and GP interests and discourages the use of subscription credit facilities to inflate a fund's internal rate of return. This approach, however, may make use of subscription credit facilities less attractive to GPs.

- Continued emphasis on fund expenses, including detailed disclosure about travel, the allocation of expenses among related vehicles, reasonable caps on organizational expenses and a comprehensive view of the expenses that should be borne by GPs, and fees and other GP compensation in addition to the management fee and carried interest,

[1] One of the underlying themes of ILPA 3.0 is the market context, which it describes as follows: "Against a backdrop of historic levels of fundraising, record distributions to LPs and rising competition for allocation, alignment between GPs and LPs, and among LPs, is exceedingly challenged at present, even as the industry more openly embraces ethical behavior and responsible investment."

all of which have received increased attention from both LPs and the SEC in recent years.

- Guidance on GP-led secondary transactions. Given the growth of the secondary market and the approaching end-of-term for many recession-era funds, ILPA 3.0 offers important structural and economic insights for both LPs and GPs.

ILPA acknowledges that ILPA 3.0 simply reflects “a synthesized view of exemplary and adoptable practices, rather than behaviors dictated by the market conditions of any particular point in time” and that it is not meant to be “applied as a checklist, as each partnership should be considered separately and holistically.” Even so, ILPA 3.0 presents useful guideposts for GPs and LPs regarding a variety of important issues in private equity partnerships.

If you have any questions regarding ILPA 3.0 or for further information about this Alert, please contact one of the following authors or your regular Hirschler contact.

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