April 25, 2022

By Email:

Vanessa A. Countryman
Secretary
U.S. Securities & Exchange Commission
100 F Street NE
Washington, D.C. 20549-1090

Re: File No. S7-03-22; Private Fund Advisers; Documentation of Registered Investment Adviser Compliance Reviews

Dear Ms. Countryman,

The Institutional Limited Partners Association (ILPA) appreciates the opportunity to comment on proposed rule S7-03-22.[1] On behalf of the approximately 585 institutional investors (LPs) and more than US$2 trillion in private equity assets we serve, we wish to thank the SEC for prioritizing the long-term success of the private markets and investing considerable time and effort in developing a robust set of market reforms that will, when implemented as suggested, help address persistent challenges experienced by LPs over the last decade.[2] We are broadly supportive of these proposals in principle and believe they will serve to further improve transparency in the private markets and enhance the ability of ILPA's members, as fiduciaries, to meet their obligations to beneficiaries.

Private Equity Remains Critical to Achieving Required Investment Returns

As we have indicated in our prior comments to the Commission,[3] private markets are a critical component of the total return of our members' investment portfolios.[4] Institutional LPs entrust private equity firms with the solemn responsibility to manage the savings and capital of individuals and organizations that rely on the returns generated by the fund's assets. The proposed enhancements to disclosures will foster greater uniformity of minimum disclosures enjoyed by all institutional LPs and will improve LPs' ability to monitor the performance of the closed-end, illiquid funds in which they invest, typically for periods of 10 years or more.

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[1] U.S. Securities & Exchange Commission, *Private Fund Advisers; Documentation of Registered Investment Adviser Compliance Reviews*, 87 FR 16886 (March 24, 2022).
[2] Institutional Investor Letter on Proposed Commission Interpretation Regarding Standard of Conduct for Investment Advisers; Request for Comment on Enhancing Investment Adviser Regulation – File No. S7-09-18
[3] ILPA Letter to U.S. Securities & Exchange Commission, *Form PF: SEC File No. 270-636* (April 30, 2018), *available at:* https://ilpa.org/wp-content/uploads/2018/04/ILPA-Comment-Letter-on-Form-PF-Collection-Request-SEC-File-No.-270-636-4.30.18.pdf; ILPA Letter to U.S. Securities & Exchange Commission Chair Jay Clayton, *Strengthening the Private Equity Market Through Balanced Oversight* (April 30, 2018), *available at:* https://ilpa.org/wp-content/uploads/2018/04/ILPA-Letter-to-Chairman-Clayton-on-PE-Regulation-4.30.18.pdf.
[4] Private Markets Rally to New Heights: McKinsey Global Markets Review 2022, McKinsey & Company, pg. 11-12 (March, 2022), *available at: https://www.mckinsey.com/industries/private-equity-and-principal-investors/our-insights/mckinseys-private-markets-annual-review*

Proposed Reforms Generally Align with Established Market Practices
ILPA considers many of the proposed reforms to be reflected in the standard practices for the majority of institutional quality private equity fund managers. Elevating and codifying market practices that work well is the logical next step for our rapidly growing and maturing industry. With clear and established minimum standards, institutional LPs and private equity firms alike will reap the benefit of clearer shared expectations and more straightforward reporting requirements.

We are pleased to share some overarching comments in addition to specific recommendations that will enhance the viability and impact of the individual proposals.[5] While ILPA's response addresses nearly all of the proposals, we have tailored our comments specifically to the application of the proposed rules to the illiquid, closed-end funds space, drawing specifically on ILPA's mandate which focuses primarily but not exclusively on the needs of institutional LPs invested in *private equity* funds. We believe adoption of the rules with specific modifications and further clarification from the SEC will provide the necessary certainty required by both managers and their LPs to avoid unintended negative consequences while achieving the stated policy objectives of this rulemaking.

Restoration of Fiduciary Duties is of Paramount Importance
ILPA is supportive of the Commission's actions to restore fiduciary duty by requiring fund advisers to be held to a fiduciary standard more proximate to that of their investors, who themselves invest in private funds as fiduciaries on their beneficiaries' behalf. ILPA has observed the widespread use of sole discretion language and expansive indemnification and exculpation provisions.[6] Taken together with the growing complexity of the private funds industry, the erosion of fiduciary duties has magnified these risks, as evidenced by the SEC's comments on persistent inadequacies in the disclosure of conflicts.

While an ordinary negligence standard would in principle be welcomed by ILPA's members, we acknowledge the unintended consequences such a standard could impose, not least being the possibility that advisers' risk tolerance will be fundamentally impacted and potentially damage the returns produced by private funds. ILPA is instead supportive of the substitution of "negligence" with "gross negligence," provided that the ordinary negligence standard applies to material breach of the LPA and side letters.

The Commission should consider prohibiting contractual provisions that expressly limit or purport to waive fiduciary duties where such a limit or waiver would result in a contractual standard of

[5] The scope of our commentary is intentionally narrow: institutionally, our members invest in both closed and open-end funds, liquid and illiquid strategies, however ILPA's mandate is oriented primarily towards private equity funds, as reflected in ILPA-issued standards and best practices. We have endeavored to comment on specific proposals with the understanding that their impacts may differ for liquid and/or open-ended funds, taking into account fundamental differences in liquidity and risk/return profiles, documentation, fee streams/economic structures and market dynamics.
[6] ILPA Follow-up Letter to Chair Gensler on Priorities for Investor Protection Reforms in the Private Funds Market Place (September 22, 2021)

care that is inconsistent with an adviser's' duty under the Advisers Act.[7] Additionally, ILPA encourages the SEC to clarify that any penalties or disgorgement resulting from an enforcement action that terminates in a settlement rather than court finding will be borne by the GP and not indemnifiable.

Reporting Requirements Will Deliver Much-Needed Transparency but Must Not Erode *Pro Rata* Investor Reporting

ILPA has encouraged industry adoption of more consistent and transparent LP-level disclosures since 2011[8] and supports the proposed rule to require registered investment advisers to disclose all direct and indirect fees and expenses quarterly. The current SEC regime has engendered an improved culture of transparency in the private funds industry, a result not possible without the engagement of the regulator. Further, ILPA has observed meaningful improvements in the quality of information being provided to LPs, in part due to adoption of the ILPA reporting standards,[9] however such practices are not yet universal across all private equity fund advisers. We agree with Chair Gensler's assessment that the proposal would "increase transparency and would provide comparability to fund investors."[10]

Across multiple statements and risk alerts, the SEC has noted issues with calculations and/or disclosures of fees and expenses, due to practices that did not conform to procedures as agreed in the investment contract.[11] Without clear and consistent disclosures, the tracking of fees and expenses charged in a private fund is exceedingly challenging. As the Advisers Act does not presently stipulate regular reporting on costs, individual investors must engage in bilateral negotiations with fund managers to secure access to this information, typically agreed through side letter agreements rather than within the Limited Partnership Agreement (LPA), which outlines information granted to all investors in the fund.[12] Investor access to basic transparency is therefore the product of market dynamics, disproportionately limiting smaller investors' access to this information.

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[7] For example, a contractual provision that permits an adviser, when exercising discretion, to consider any interests, including its own interests, should be impermissible unless there are contractual assurances that the adviser would not act inconsistent with the best interests of the fund or put its own interests ahead of those of the fund.

[8] ILPA Quarterly Reporting Standards, available at https://ilpa.org/capital-call-distribution-quarterly-reporting/; ILPA Fee and Expense Reporting Template, Institutional Limited Partners Association, available at: https://ilpa.org/reporting-template/

[9] A list of LP, GP and service provider organizations that have endorsed the ILPA Reporting template is available at https://ilpa.org/reporting-template/template-endorsers/. In 2021, 59% of LPs reported receiving the ILPA Fee Template at least 50% of the time: *see* https://ilpa.org/wp-content/uploads/2021/10/Key-Findings-Industry-Intelligence-Report-Fund-Terms.pdf

[10] Chair Gensler, Statement on Private Fund Advisers Proposal, US Securities and Exchange Commission (February 9, 2022)

[11] Spreading Sunshine in Private Equity., U.S. Securities & Exchange Commission (May 6, 2014), https://www.sec.gov/news/speech/2014--spch05062014ab.html; Div. of Exams, Risk Alert: Observations from Examinations of Private Fund Advisers (Jan. 27, 2022), https://www.sec.gov/files/private-fund-risk-alert-pt-2.pdf; Div. of Exams, Risk Alert: Observations from Examinations of Investment Advisers Managing Private Funds (June 23, 2020), https://www.sec.gov/files/Private%20Fund%20Risk%20Alert_0.pdf).

[12] In 2020, only 8% of LPs indicated that a commitment to provide the ILPA Reporting Template was included in the LPA for all investors' benefit; 75% indicated the commitment was typically either made through the side letter or informally and not reflected in fund documents at all, https://ilpa.org/wp-content/uploads/2020/06/ILPA-Industry-Intelligence_Private-Market-Fund-Terms-Survey_2020.pdf

We further believe that the Commission could improve the proposal by preserving LP-level disclosures where the adviser has agreed to provide them and requiring managers to make such LP-level reporting available to those investors who request it. As proposed, the rule would require the disclosure of fees and expenses at the fund level. However, many institutional investors require, and have successfully negotiated for fee and expense reporting provided at the *pro rata* individual investor or limited partner (LP) level. This information is essential for ILPA member institutions who are required to provide an annual accounting of all investment costs to their own beneficiaries or governing bodies, often on a fiscal year cadence that does not align with annual reporting by the manager.[13]The SEC rule should not erode what has become market practice among many institutional investors and their managers by erecting a maximum compliance threshold rather than a minimum standard. We therefore respectfully request the Commission consider improving the final rule by requiring private fund advisers to make fee and expense reporting available at the *pro rata* level, upon the investor's request. Further, we encourage the Commission to confirm that in cases where managers already provide standardized reporting such as, but not limited to, the ILPA Reporting Template they have satisfied the requirements of the rule, obviating the need to provide additional fund-level reporting and preventing against managers electing to provide fund-level reporting alone. With this proposal, we believe the Commission is creating the conditions for market-wide adoption of established industry reporting standards such as the ILPA Reporting Template, which was expressly designed to capture cost information for private equity funds.[14]

Side Letters are an Essential Tool for LPs–Clarification of Material, Negative Impact of Preferential Terms is Necessary

ILPA is supportive of greater transparency in the industry. However, we are concerned that the rule concerning preferential treatment as proposed could have unintended consequences. Side letters are essential to LPs' ability to invest in private funds, as a means of securing critical governance, statutory, or regulatory protections that provide institution-specific benefits otherwise not included in Limited Partnership Agreements. These institution-specific provisions, such as statutory requirements, regulatory guarantees and Advisory Committee seats, do not harm or otherwise impact other investors in the fund. Without these provisions, the majority of institutional LPs would not be able to invest in private funds,[15] the returns from which are necessary to meet their organizations' investment objectives and obligations.

As proposed, the facts and circumstances standard for determining material, negative impacts for preferential redemption rights or transparency may impede LPs' ability to negotiate for side letters.

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[13] In certain jurisdictions, public pensions are required to produce such disclosures annually, e.g., California Assembly Bill 2833 (2016); Texas Senate Bill 322 (2019). LPs subject to such requirements typically include language in their side letters to secure the necessary information to satisfy legislated reporting obligations.

[14] ILPA Reporting Template, *available at*: https://ilpa.org/reporting-template/. The ILPA Template was expressly designed to reflect direct and indirect fees, offsets, partnership expenses and carried interest charged by private equity advisers and their affiliates.

[15] A survey conducted at the 2020 ILPA Private Equity Legal Conference found that 76% of ILPA members would not invest in a private equity fund without a side letter. *See* 2020 ILPA Private Equity Legal Conference, Institutional Limited Partners Association (October 2020), available at: https://ilpa.org/document-library/2020-ilpa-private-equity-legal-conference-lp-perspectives-deck/

GPs are likely to take a conservative view on what the SEC may deem material, negative impacts and are anticipated to resist making side letters available in future funds as a result.

We urge the Commission to provide greater specificity as to the nature of terms deemed to have a material, negative impact on other investors in the same fund. We acknowledge that side letters may also capture economic incentives that align with the size of an individual LP's commitment to a private fund or the timing of their entrance to the fund, i.e., as a seed or first-close investor; other LPs in such funds do not deem such differentiated treatment to be damaging but rather an accepted market practice consistent with contract negotiations in all domains and not limited to private fund investments. So long as such agreements are known and disclosed through the Most Favored Nation (MFN) process, ILPA's members do not consider preferential rights or economics tied to fund commitment size or participation as a seed or anchor investor to fall within the preferential treatment having material, negative impact on other LPs in the fund.

Further, we request that the SEC clarify that this rule does not prohibit investors from entering into bespoke arrangements with private fund advisers to secure essential institution-specific requirements.

Finally, we observe that the requirement to provide written notice of preferential terms to prospective investors would be procedurally misaligned with the MFN process that runs after the final close of a closed-end fund. In most closed-end fund negotiations, side letters are negotiated up to the final moments before the fund's final close, therefore disclosures of side letter terms before this point in the negotiation process would be an inaccurate and incomplete reflection of the provisions secured by other LPs in the fund. Without a clearer definition of what constitutes a prospective investor, or a specific minimum notice window, LPs might receive disclosure that is technically in advance of their subscription to the fund but coming in as little as mere minutes before the fund's final close, offering little to no utility in shaping the LP's negotiating priorities. We encourage the Commission to consider the distinctions between open-ended and closed-end funds in elevating existing industry best practices around disclosures to current and prospective investors and would recommend a best-in-class MFN process for closed-end funds as a means to satisfy the desired policy objectives in the context of closed-end funds, rather than advance or annualized notices yielding less timely or less actionable information.

Aside from Quarterly Statements and Fund Audits, Implementation Timetables Should Apply on a Go-Forward Basis

The scope of the proposals is broad, with certain proposals requiring changes in behavior and operating norms while others would require amendments to fund documentation. Each individual proposal presents a range of cost and timing considerations for implementation. ILPA believes that the proposed reforms, with the exception of required quarterly statements and annual fund audits, should be solely applied to new funds formed after the implementation date, to avoid the necessity of renegotiating existing fund agreements, side letters and subscription agreements, the cost and uncertainty of which would be borne by LPs. ILPA also supports consideration of an extended implementation timeline for smaller or newer managers that require more time to modify practices to comply, as determined through specific parameters or a combination thereof such as assets under management, headcount or maturity of the platform.

With implementation of the quarterly statement requirements, the implementation timeline should consider the necessary procedural and infrastructural adaptations required among managers with less robust LP-facing reporting capabilities today. To optimize the balance between incurred costs and the information benefits to LPs' evaluation of prospective investments in existing or new managers, ILPA encourages the SEC to consider requiring compliant quarterly reporting within a reasonable lookback period, e.g., 2018 fund vintages and later.[16] Mandating the recasting of historical fees and expenses or performance beyond a sensible period would create meaningful costs but would be of dubious benefit to LPs.

Private equity has delivered enormous long-term financial benefits to LPs, and by extension, the millions of people and essential programs they serve. The investment and operating model is not, in our view, fundamentally flawed or irreparably broken. However, market forces have, over the past decade, eroded elements of the partnership between LPs and advisers. This has coincided with the emergence of certain practices that must be addressed for the industry to thrive and continue to deliver superior investment results. With a thoughtful, deliberate and principles-based implementation of the proposals, subject to the specific modifications we suggest herein, ILPA views the reforms as central to ensuring this next phase of the private markets development benefits all industry stakeholders. Given private funds' impact on society, whether through the quantum of saver's capital managed or the number of privately held companies touched, such reforms are a worthy endeavor for the Commission.

In case of questions or to request additional information, please contact ILPA's Managing Director, Industry Affairs, Jennifer Choi, at [redacted]

Sincerely,

Steve Nelson
Chief Executive Officer
Institutional Limited Partners Association (ILPA)

[16] Vintage year should be defined as either the year of the investment vehicle's first drawdown or capital call from its investors; or the year when the first committed capital from outside investors is closed and legally binding. Source: GIPS Standards for Firms, 2020, available at https://www.cfainstitute.org/-/media/documents/code/gips/2020-gips-standards-firms.ashx

Recommendations Specific to Individual Rule Proposals

Quarterly Statements

ILPA's comments on the quarterly statements proposal are specifically through the prism of private equity fund disclosures. ILPA has strongly encouraged industry adoption of more consistent and transparent reporting, calibrated to the LP level, since 2011 – including capital account statements, capital call and distribution notices, quarterly reporting and fee and expense disclosures.17 ILPA has encouraged the industry to move towards more detailed standardized reporting as opposed to the more typical presentation of net figures with no itemized accounting for fees, offsets applied or partnership expenses by category.

ILPA has also advocated for detailed quarterly reporting, rather than annual reporting alone, to ensure that investors whose fiscal year ends do not align with the calendar year can both validate that fees charged conform with contractual agreements and report fees and expenses paid to their own stakeholders.[18]

ILPA is pleased to have observed meaningful changes in the quality of information being provided by managers to investors,[19] however such practices are not yet universal across all private fund advisers. Currently, advisers most often agree to certain disclosures on costs through side letters, which benefit only the requesting individual LP, or through informal agreements not captured in fund documents.[20]

The size and/or sophistication of the requesting investor are no guarantee of fulsome disclosures. Some fees are reported "so deeply in the partnership agreements and financial reporting that it becomes cumbersome for public funds to identify the full breadth of fees and expenses and disclose them."[21]

Despite these improvements, the SEC has continued to enumerate deficiencies in how fees and expenses are allocated and disclosed, both at the fund and portfolio company level or by the adviser and/or its affiliates.[22] As such, ILPA's members have concluded that voluntary disclosure alone will not yield satisfactory results; regulatory intervention is needed to erect and enforce a minimum disclosure standard.

The fund-level reporting that the SEC has proposed is a reasonable minimum expectation; it is inconceivable that advisers are not maintaining adequate accounting of fees, offsets, expenses, accruals and the like at the fund-level, even if the information is not disclosed today. By removing

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[17] *Supra 8.*

[18] NAST resolution endorsing ILPA template: https://cdn.ymaws.com/member.nast.org/resource/collection/660A9E8A-F78C-47A8-8AA3-DFF05472EB70/Final_2019_SUPPORTING_POLICIES_TO_INCREASE_FEE_DISCLOSURE_AND_STANDARDIZE_REPORTING_OF_PRIVATE_EQUITY_INVESTMENTS.pdf

[19] Industry Intelligence Report: What's Market in Fund Terms., ILPA (2021) available at: https://ilpa.org/wp-content/uploads/2021/12/2021-ILPA-Industry-Intelligence-Report-What-is-Market-in-Fund-Terms.pdf

[20] *Ibid.*

[21] *Supra 17.*

[22] U.S. Securities & Exchange Commission, Risk Alert, OCIE, Observations from Examinations of Investment Advisers Managing Private Funds (June 2020)

minimum disclosures as a feature of fund negotiations, LPs would be permitted to devote their energies and negotiating capital to other provisions, including fund governance.

ILPA also considers the principles-based approach on cost disclosures as outlined by the Commission in the release to be appropriate and sufficiently flexible to apply to the full breadth of private fund strategies as well as accommodating the evolution of these products and market practices over time.

Enhancements to the Proposal

As proposed, requiring fund-level disclosures would create a helpful minimum standard, particularly where such information is not being consistently provided to LPs. However, for many ILPA members, fund-level disclosures alone would be both insufficient for their own monitoring and reporting requirements as well as a regression from the level of reporting they currently receive. Further, many of the benefits that the SEC references in the release cannot be fully achieved with fund-level information alone. Examples of cases in which fund-level reporting would be insufficient include: individual LPs that have opted out of specific investments for ESG exclusion policy reasons, e.g., carbon-related industries or armaments; LPs that have requested to be excluded for the purposes of underwriting subscription facilities and opting instead for more frequent capital calls; LPs that have negotiated specific fees or percentage offsets. In such cases, fund-level reporting would be insufficient as a check against the charges provided for in the LPA and side letter.

ILPA recommends amending the proposed rule to ensure that fund-level reporting requirements serve as a minimum expectation and not a maximum compliance threshold, particularly in cases where managers currently provide LP-level information or LP-specific disclosures to satisfy specific statutory or regulatory requirements in their respective jurisdictions. The rule should not be interpreted as supplanting or reverting LP-level disclosure obligations as agreed by the GP. We therefore respectfully request the Commission consider improving the final rule by requiring private fund advisers to make fee and expense reporting available at the *pro rata* level, upon the investor's request. Beyond the proposed fee and expense reporting requirement, we also note that the elements as outlined in the Statement of Contributions and Distributions represent a step back from what LPs are accustomed to receiving today.

ILPA appreciates that the SEC is not seeking to create a new template or standard and is instead looking to existing widely adopted industry standards for reporting on costs. Standardized definitions and taxonomy will be necessary to achieve the objective of apples-to-apples comparisons on costs, to avoid the current practice of categorization of costs as "other" but may not be achievable where underlying assets or strategies are fundamentally discrete. ILPA encourages the SEC to recognize reporting that conforms with established standards, including but not limited to ILPA's templates, would satisfy the rule.[23] To be clear, ILPA is not proposing that the ILPA template should be required of all private fund advisers, as the template was

[23] *See:* National Council of Real Estate Investment Fiduciaries and the Pension Real Estate Association (NCREIF PREA) Reporting Standards, *available at:* https://www.ncreif.org/reporting-standards/ InvestEurope Investor Reporting Guidelines, *available at:* https://www.investeurope.eu/industry-standards/professional-standards/investor-reporting/ Standard Boards for Alternative Investments (SBAI) Standards, *available at*: https://www.sbai.org/resource/standard-excel.html

developed specifically for private equity and not calibrated to the specific charges of venture capital or private credit funds, for example. Nor do we suggest that all investors in all private fund strategies will require quarterly, LP-level reporting; ILPA recognizes that investors in smaller funds or in certain strategies such as venture capital may have differentiated requirements. Similarly, we acknowledge the importance of a transition period for advisers whose reporting practices today do note align with the proposed requirements.

We recognized that for advisers lacking robust LP-facing reporting today this will involve some degree of investment, the cost of which will be borne by LPs, either directly as a partnership expense or indirectly through higher management fees. As indicated in our comments below on the prohibition of certain fees and expenses, ILPA respectfully requests that the SEC confirm that costs associated with satisfying the proposed quarterly reporting requirements would not be considered a prohibited compliance cost, as LPs would benefit from this enhanced reporting and could reasonably be expected to bear a *pro rata* portion of such costs, particularly in cases where the reporting is provided by a third-party fund administrator and approved by LPs within the LPA as an allocable partnership expense. We also recognize that the additional costs associated with satisfying the enhanced scope and frequency of reporting would be challenging for smaller managers to absorb under the management fee; forcing such costs to be borne by the adviser in every circumstance may present the unintended consequence of erecting barriers to new fund formation and a resulting consolidation among the largest advisers with the most robust reporting capabilities.

While a principles-based approach to cost disclosures makes sense, for performance disclosures the diversity of methodologies and formats would suggest the need for, as the Commission has proposed, a standardized approach including clear definitions and taxonomy. ILPA encourages the SEC to require additional disclosures around methodologies and assumptions in use and to require advisers to make available upon request the full calculation breakdowns across the various data points covered in the quarterly statement rule provision.

The proposed requirement for distribution of fund-level information within 45 days of quarter close is appropriate for traditional private equity managers for all but fiscal year-end reporting, whereby 90 days or more following the stated fiscal year end of the fund is the accepted market standard. More time may be required in cases where the GP is honoring commitments to provide individual LPs with specific or *pro rata* reporting, as agreed per fund documents. Funds of Funds and Secondary Managers should be provided additional time, e.g., 14 days as with AIFMD, to prevent routine instances of providing previous quarter-end data to fulfil SEC requirements.

ILPA believes that the implementation guidance should encompass a reasonable lookback period, e.g., 2018 fund vintages and later, aligned with broader industry trends around adoption of reporting standards such as the ILPA reporting template.[24] Mandating the recasting of historical fees and expenses or performance to this point would optimize the benefit for LPs with minimal

[24] Vintage year should be defined as either the year of the investment vehicle's first drawdown or capital call from its investors; or the year when the first committed capital from outside investors is closed and legally binding. Source: GIPS Standards for Firms, 2020, available at https://www.cfainstitute.org/-/media/documents/code/gips/2020-gips-standards-firms.ashx

implementation costs. ILPA considers the effort required to comply with the proposed rule should be manageable within a fixed time period as the biggest differences to account for will relate to adding back expenses to compute a gross IRR, MOIC calculation with a slightly altered methodology, and/or providing performance metrics both with and without the impact of the subscription line.[25]

Performance Disclosure

Specific, defined methodologies for standardized performance metrics would be a welcomed improvement for the industry. Currently, it can be difficult for LPs to compare performance metrics across different advisers due to distinctions in methodologies, assumptions and caliber of disclosures. We would encourage the SEC to more precisely define "illiquid fund" to capture strategies such as Private Credit, e.g., Income generating portion of assets, not just a focus on return of proceeds.

We consider the performance metrics outlined within the proposal to be critical for LPs' understanding of comparative private equity performance: gross and net IRR and MOIC, including for both realized and unrealized portions of the illiquid fund's portfolio, with realized and unrealized performance shown separately. We support requiring performance metrics disclosed "without" the impact of any fund-level subscription facilities but to have maximum impact encourage the SEC to require the disclosure "with" the impact of fund-level subscription facilities as well. We recommend the Commission consider exemption advisers from presenting performance without the impact of subscription lines where the days outstanding for the fund is typically less than 120 days, i.e., facilities are being used solely or primarily to streamline capital calls and not enhance reported IRR performance.

ILPA also recommends the SEC consider periodicities in addition to Inception to Date (ITD), namely Calendar Year to Date (CYTD) and Inception to Prior Year's End. As the industry migrates to a universally agreed, and ideally global, standard, in the interim, setting more concrete minimum standards for disclosure of the assumptions and methodology used would be beneficial to investors.

While ILPA supports progress towards a standardized methodology for performance presentations, we believe a clear delineation of treatment of various fee, expense and contribution types is essential to achieve maximum impact. As illustrated by the methodologies sampled below, the calculation of standard performance metrics such as Money on Invested Capital (MOIC) and Distribution to Paid-in Capital (DPI) can vary meaningfully adviser to adviser, inhibiting true apples-to-apples comparisons.

[25] Upon the issuance of the ILPA Reporting Template in 2016, subscription credit facilities were less common than today; in just a matter of years, such facilities are now effectively universal, with 98% of funds having the ability to put a credit facility into place according to the 2021 ILPA Fund Terms Survey, available on file with ILPA.

Sample Treatment of Various Cash Flows for MOIC and DPI Calculations

	GP1	GP2	GP3	GP4	GP5	GP6
Contribution	Denominator	Denominator	Denominator	Not clear	Denominator	Denominator
Distribution	Numerator	Numerator	Numerator	Denominator	Numerator	Numerator
Recallable Distribution	Numerator	Numerator	Numerator	NA	Numerator	Numerator
Early Interest Payment (LP in later closing)	Denominator	Denominator	NA	NA – outside fund expense	Denominator	NA – outside fund, not in calculations
Early Interest Distribution (LP in earlier closing)	Numerator	Denominator	NA	NA – outside fund expense	Numerator	NA – outside fund, not in calculations
Management Fee	Denominator	Denominator	Denominator	Numerator	Denominator	Generally withheld from distributions; if called, denominator
Advisory Fee	Denominator	Denominator	Denominator	Numerator	Denominator	Generally withheld from distributions; if called, denominator
Return of Excess Contribution (including rebalancing after subsequent closings)	Denominator	Denominator	Denominator	Denominator	Denominator	Subsequent closes are outside the fund, not included in calculations
Recall of Excess Distribution (reallocating prior distributions after subsequent closing)	Numerator	Denominator	Numerator	NA or varies	Numerator	Subsequent closes are outside the fund, not included in calculations
Recall of Excess Recallable Distribution (reallocating prior recallable distributions after subsequent closing)	Denominator	Denominator	Numerator	NA or varies	Numerator	Subsequent closes are outside the fund, not included in calculations
Return of Bridge Loan	Numerator	Denominator	Denominator	NA or varies	Denominator	If called to repay a bridge loan, denominator
Tax Withholding (reduction to taxable LPs vs tax exempted LPs)	Numerator	Numerator	Numerator	NA or varies	NA	Numerator

In light of the disparate treatment of specific cash flows as indicated above, including recallable distributions, excess contributions and excess distributions, while ILPA is favor of embracing a recognized standard such as GIPS, we encourage the SEC to require that advisers "show their work" in specific terms in calculation of the required performance disclosures indicated in the final rule. We also respectfully request that the SEC confirm that any mandated disclosures would not supersede or obviate preferred LP-specific performance disclosure formats as agreed through side letters or the LPA.

Performance metrics have widespread implications, including across different industry benchmarks, benchmark providers, compensation policies at LP and adviser organizations, accounting practices (including for LPs that are government organizations and must follow certain guidelines), and historical research and academic papers. There are also different methodologies based on both LP preferences and adviser preferences on how to view these performance metrics, with multiple assumptions built into the various elements. As such, ILPA supports moving to a reporting requirement with standardized performance metrics but encourages the Commission to provide in the rule text and interpretative guidance clear definitions for each term drawing on current market practices and understanding.

Mandatory Private Fund Adviser Audits

ILPA is supportive of the annual audit requirement, which we believe is critical to ensuring that the assets of the fund are protected from fraud and malfeasance. ILPA welcomed the 2013 SEC guidance preserving exemptions from the Custody Rule, and eliminating the cost of retaining a custodian, by allowing managers to undergo an annual financial statement audit as an alternative to the surprise examination requirement.26 ILPA believes the practice of an annual fund audit to be mainstream among the vast majority of institutional quality managers today. We note that this rule would effectively alter the exemption under the Custody Rule and believe that compliance with the audit requirement under this rule proposal should satisfy the Custody Rule as well.

We recognize there are fact patterns in which a fund audit would imply cost in excess of any benefit to LPs. We recommend the SEC consider exemptions under the following circumstances: subadvisers where the manager plays no role in valuing assets or receives little to no compensation; funds below a *de minimus* AUM threshold; funds with a *de minimus* number of remaining investors; cases where an exemption from the audit has been approved by the LPAC and/or a majority of LPs by interest. For funds past term and beyond the final term extension, the surprise exam requirement under the Custody Rule should hold.

While ILPA understands that auditing “friends and family” co-investment vehicles presents additional costs and only marginal benefit to LPs in the commingled fund, such vehicles are already exempted from the Custody Rule. It is worth noting, however, that no oversight mechanism exists, short of an SEC examination, to ensure that such vehicles are not operating in conflict with the fund, e.g., shifting broken deal or other expenses to the primary fund investors. In contrast, co-investment vehicles, typically created around interests in a single asset, may be structured on a no-fee/no-carry basis and generate little to no compensation for the adviser but related auditing costs for such vehicles should be minimal. For certain LPs, such as insurance companies, audited financial statements must include co-investment vehicles and feeder funds to be counted as an Admitted Asset for inclusion on the insurer’s regulatory balance sheet, otherwise treated as a total capital loss which impacts an insurer’s regulatory capital.

We believe the private funds rule should align with the Custody Rule, in that the adviser would be deemed to comply with the surprise examination requirement as long as audited financial statements are prepared in accordance with US GAAP and distributed to all limited partners. IN cases where the audited financials are not prepared in accordance with US GAAP, the adviser would be required to distribute a reconciliation to US GAAP along with its audited financials. The timelines for distribution of the audited financial statements should also align with the Custody Rule, i.e., in most cases, within 120 days of the adviser’s fiscal year end, and up to 180 days for funds of funds and 260 days for funds of funds of funds, although certain regulated LPs may be subject to timelines of less than 120 days, e.g., best efforts basis to distribute within 90 days.

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[26] Final Rule: Custody of Funds or Securities of Clients by Investment Advisers; Release No. IA-2176; File No. S7-28-02; SEC.gov | Staff Responses to Questions About the Custody Rule

We are also supportive of the requirement of an audit upon the fund's liquidation, as these processes can take years. The audit is essential to ensure remaining assets are being protected from a manager under stress.

ILPA is supportive of the proposed independence requirements for the accountants performing the audit as well as the requirement to notify the Commission, upon completion of the audit, of any modified option or termination or dismissal of the auditor.

While the proposed rules do not address the scope of the fund audit itself, ILPA believes that currently such audits deliver procedural comfort but fall short of true assurance. Few fund audits conducted include a recalculation of the waterfall or sample testing of LP capital account statements to verify that the fees and expenses charged to a subset of individual LPs conform with the LPA and side letters. As any expansion of the scope of the fund audit would impact the timeline for delivery of audited financial statements to LPs, ILPA is not proposing here that such a change be made but will continue to encourage the industry to consider opportunities to enhance the value of the audit to LPs.

Adviser-Led Secondaries

ILPA supports the provision requiring the use of a fairness opinion in adviser-led secondaries but with modification, as LPs generally deem fairness opinions to offer procedural comfort but not true assurance of fair pricing of the transacted assets. Other methods, such as through a partial disposition to a third-party or an arms-length transaction through a minority stake sale to another adviser and independent of the proposed secondary are perceived to yield more valuable information on the fairness of the pricing offered.[27] ILPA encourages the SEC to consider such mechanisms, if conducted within a fixed period, e.g., 12 months, preceding the solicitation of LPs' participation in the secondary, as satisfying the requirements of the rule and obviating the need for a fairness opinion, particularly in cases where the rationale for such an alternate process has been disclosed and approved by the LPAC as a substitute for, or complement to, a fairness opinion.

Regardless of the methodology used, the SEC should specify the timing required, e.g., a presumption of reasonableness if an adviser provides the pricing information, and other relevant information governing the transaction, with 20 business days' notice; as written, "prior to the closing of the transaction" does not ensure sufficient time for LPs to act on the information in the decision to roll or sell their interest in the transacted asset(s). ILPA also encourages the SEC to clearly define the characteristics of an adviser-led secondary, in that LPs are seldom offered a status quo option, meaning that the transaction itself does not occur. Rather, such secondaries typically force LPs to choose between being buyers of the asset(s), by participating in the new

[27] In an ILPA survey of members conducted on 24 February 2022, 49% indicated a fairness opinion should be a required element of the valuation process for a continuation fund transaction, 77% indicated a third-party valuation should be required and 39% supported requiring an arms-length transaction via minority stakes sale to another adviser (respondents asked to select all that apply). Only 1% believed a fairness opinion would completely fulfill their needs from a governance perspective, while 58% indicated that such opinions check a governance box but do not afford the preferred level of insight, and 35% indicated fairness opinions provided insufficient information for them to feel comfortable with the valuation. Presentation on file with ILPA

structure created, at new terms and often with additional fees charged, or as sellers, by fully liquidating their interest in the asset(s).

While we are encouraged by the SEC's engagement on the need for validation of the value of the transacted assets, ILPA believes the most meaningful shift in market practice would be to address the conflicts of interest involved in adviser-led secondaries more broadly, which often extend well beyond pricing. ILPA members have observed that, as LPs in the original funds being transacted, the secondary is often structured in such a way that the benefits disproportionately accrue to the adviser and in some cases the new buyers relative to the LPs in the existing fund. ILPA has asserted that the terms of the adviser-led secondary should be no worse for rolling LPs, i.e., those existing LPs transacting as buyers in the secondary, than in the original LPA, and that existing LPs should not be disadvantaged relative to their status prior to or absent the transaction.[28] While understandably beyond the scope of the SEC's mandate or the rules proposed in this case, ILPA observes that the most meaningful shift in market practice would result from addressing the rationale for the transaction, including the age and status of the transacted asset(s), the timing and quality of disclosures to the LPAC and the LPs in the existing fund regarding the process surrounding the transaction, and the process for securing LP and/or LPAC approvals and/or conflict waivers. ILPA continues to believe that rolling LPs should be afforded the option to participate in the adviser-led secondary as buyers but with no change in economic terms, recognizing that doing so while retaining the LP's original *pro rata* share in the transacted asset cannot be guaranteed.

The SEC has asked whether the fairness opinion should "cover all, or certain other, terms of the transaction." ILPA considers the scope of the fairness opinion to be limited to the imputed value of the assets and not the broader contours of the transaction such as the fees being charged, or specific rights granted to investors participating as buyers in the new entity created by the secondary transaction. ILPA has recommended the use of independent advisers, not fairness opinion providers, who can counsel the LPAC in their consideration of how such a process is run, such as the process for soliciting buyer offers on the transacted assets.[29]

ILPA is supportive of the requirement that the fairness opinion should come from an independent provider and a summary of any material business relationships should be provided. While the majority of these services today are provided by firms that specialize in valuation services, in cases where the provider offers other services, such as an accounting firm, ILPA believes disclosure of the amount of fee revenue represented by the provider's advisory engagement on the secondary transaction relative to revenue generated through the provider's relationship with the firm should be sufficient. ILPA is also supportive of the requirement that advisers maintain a record all information distributed to investors related to the Adviser-Led Secondary.

Prohibited Activities

Fees for Unperformed Services

[28] GP-led Secondary Fund Restructurings, Considerations for Limited and General Partners, Institutional Limited Partners Association (April 2019), available at: https://ilpa.org/wp-content/uploads/2019/04/ILPA-Guidance-onGP-Led-Secondary-Fund-Restructurings-Apr-2019-FINAL.pdf

[29] *Ibid.*

ILPA supports the provision prohibiting the collection of fees from the fund or a portfolio investment for services that are never ultimately rendered. We agree with the approach that if an adviser is paid in advance for services it reasonably expects to perform, but ultimately does not provide the services, that the adviser is required to refund the prepaid amount attributable to the unperformed services.

Certain Fees and Expenses

ILPA is supportive of the intention behind this proposal, namely the clarification of which costs associated with compliance should reasonably be borne by the advisers versus allocable to the partnership but is not supportive of a broad and blanket prohibition on the allocation of all compliance-related costs. We anticipate that, without an appropriately defined scope, such a prohibition would pose challenges for advisers in discerning between costs related to the adviser's activities versus those of the fund and will likely result in higher management fees and without the benefit of itemized disclosure as to the actual compliance-related costs absorbed by the adviser.

ILPA members have observed a trend over the last decade of increasingly expansive disclosures in Form ADV and within the operating expense and indemnification provisions of the LPA, covering a myriad of potential costs that may be charged to the partnership subject to any carveouts for bad acts. ILPA considers the initial registration with the Commission and filings such as Form PF and ADV to be establishment costs that should be reasonably borne by the adviser.[30] While it is market practice today for such costs to be allocable, within specific limits, to the partnership, and for ongoing costs related to compliance to be charged to the partnership as an expense, it is possible that some advisers do not allocate those costs to the partnership. Due to insufficient itemized disclosure of such costs the total and typical quantum of actual charges is unclear. We agree that any compliance costs paid should be disclosed and transparent to all LPs, whether or not allocable as a fund expense and support the prohibition on charging the fund for costs associated with responding to an examination or investigation of the adviser and its related persons, although we understand that in many cases such costs may be treated as reimbursable legal expenses. The SEC should make it clear that the cost of any remediation resulting from any regulatory exam or review should be borne by the adviser, including any disgorgement and/or penalties that follow from such exams and any resulting enforcement actions.

As a matter of principle, ILPA considers certain costs essential to the operation of the firm, such as salaries to maintain a compliance function, software and travel related to deal sourcing, to be reasonably borne by the adviser as these are overhead costs that the management fee is intended to pay for. To further illustrate how the SEC might clarify which compliance related costs are allocable to the partnership versus borne by the adviser, In cases where an adviser engages a third party to review compliance protocols, including conducting "mock exams", ILPA would consider such costs to provide the adviser with instruction on enhancements to firm operations, the benefits of which would surpass the management of any individual fund.

While only a minute percentage of all examinations result in enforcement actions, a significant majority of all examinations result in a deficiency letter that enumerates specific shortcomings in

[30] ILPA Principles 3.0, Institutional Limited Partners Association, (June 2019) available at: https://ilpa.org/ilpa-principles/

compliance protocols, in the adviser's conformance with the LPA or side letter, or inadequate disclosures. In all cases, the adviser is directed to address these deficiencies by SEC examinations staff, in some cases to avoid an enforcement action. These are not matters of malfeasance or impropriety but often inadequacies in hygiene; it is inconceivable that the LPs in the fund should bear the cost of such remedies, which point squarely to the cost of doing business as an adviser presumably offset through the management fee revenue collected from the LPs. In cases where the adviser elects to settle with the SEC as opposed to a conclusive finding or admission of wrongdoing, allocating such costs to the partnership is even more unfathomable.

ILPA encourages the SEC to confirm which specific costs associated with complying with the final rules should be borne by the adviser. ILPA believes that certain costs implied by the proposals, such as the required quarterly statements and the annual fund audits, are in many cases allocable to the partnership today per fund documents. In the case of the proposed enhanced reporting that would allow for more robust monitoring and apples-to-apples comparisons because LPs would benefit, it is reasonable that such costs should be borne by the partnership under many scenarios. More than half of advisers utilize outsourced fund administration services to produce quarterly and annual reporting; where the LPs have approved the allocation of such third party costs as a partnership expense within the LPA, ILPA is supportive of the continuation of this practice.[31] Where such reporting is produced internally, ILPA does not support the allocation of a portion of staff salaries to the partnership and believes instead that all salaries should be covered by the management fee.

ILPA recognizes that proscribing the pass-through of compliance costs broadly considered as a partnership expense could yield unintended consequences, chiefly increased management fees. Shifting to a budget-based management fee may be an alternative approach worthy of serious consideration; for GPs that provide adequate transparency to LPs as to the nature and quantum of costs covered by the management fee within a mutually agreed fee percentage and basis for calculation, additional periodic disclosures and itemization would become less necessary; such an approach would also lessen the ambiguity around how GPs would treat certain activities in the context of regulatory compliance charges absorbed under the management fee versus expensed to the partnership. The predictability of the management fee, particularly if coupled with approval rights, could also serve as a useful mechanism for alignment of interests and cost containment.

Reducing Adviser Clawbacks for Taxes

ILPA is supportive of the intention behind this provision, which addresses the leakage experienced by LPs due to hypothetical tax withholding rates being applied to clawback distributions that unreasonably exceed the actual tax rates that would be incurred by the affected individual(s). Prohibiting an adviser from reducing a clawback distribution by any actual, potential or hypothetical tax would improve alignment of interest between LPs and GPs by creating a disincentive to enter a clawback situation. "All capital back" waterfall structures, also known as a European waterfall, maximize alignment in part by minimizing clawback liabilities, however we recognize that such structures are not the prevalent market standard.

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[31] Fund Administration Report 2021, Private Equity International (May 31, 2021) available at: https://www.privateequityinternational.com/fund-administration-2021/

ILPA also observes that, as the result of a prohibition on reducing clawbacks for taxes, the provision could yield unintended consequences harmful to LPs, in that waterfall provisions in future fund documentation may be structured to eliminate the clawback, managers would seek to limit clawback events or to slow distributions over time to limit tax exposure, particularly smaller managers less able to bear such exposure or uncertainty. We acknowledge that in cases where taxes are paid on a liquidated basis, employees that participate in the carry distribution incur tax liability and receive a tax distribution; those distributions would need to be clawed back as well, which may create operational complexity.

Short of a total prohibition on reducing clawback distributions to LPs by tax withholdings, ILPA would be supportive of an amended rule that allows for a reasonable hypothetical rate, provided the following conditions are satisfied: the rate is as applied to individual members of the adviser impacted and the rationale for the applied rate is disclosed in plain English to LPs. The tax treatment should account for loss carryforwards and carrybacks, the character of the fund income and deductions attributable to state tax payments, and an ordinary deduction or loss as a result of any clawback contribution or related capital account shift. We also believe that fund documents should stipulate disclosures to LPs regarding the allocation of clawback distributions among LPs beyond the term of the fund, particularly where individual LPs, for tax reasons such as UBTI, are unable to accept such distributions.

For the sake of simplicity, we believe that any provisions in the final rule addressing the clawback should apply only to new funds formed after the implementation date, so as to avoid the need for renegotiation of fund documents and to reduce the risk of amended tax returns or partnership audits.

Limiting or Eliminating Liability for Adviser Misconduct

ILPA is generally supportive of reining in what have become mainstream practices in fund documentation egregiously shifting the risk burden to the fund's LPs, reducing the standards of care or loyalty and giving the GP sole discretion to consider their own interests above those of the fund, GP bearing little to no accountability, even for malfeasance or gross negligence. Sophistication or size is no balm, nor guarantee of an individual investor's ability to secure certain protections, including interpretation of specific provisions such as fiduciary duty.[32] We believe a minimum standard fiduciary duty must be codified in securities law rather than left to the vagaries of the market; private funds are no exception to this.

Many of ILPA's largest and most sophisticated members, with private markets AUM in the tens of billions, are frequently called upon to waive their fiduciary duties to invest in private equity funds run by advisers who have maximally waived and disclaimed theirs. These LPs frequently negotiate for language in the LPA to counter a diminished standard of care in the LPA. Such language typically includes an attestation by the manager that they will take the interests of the partnership as a whole into account; that in all cases, standards of good faith and fair dealing (under Delaware law) will remain intact; and confirmation that the adviser is subject to the fiduciary duty as outlined in the Advisers Act. While such remedial language creates an obligation between

[32] Leo E. Strine Jr. and J. Travis Laster, The Siren Song of Unlimited Contractual Freedom, Harvard University John M. Olin Center for Law, Economics and Business, Discussion Paper No. 789, P. 3, August 2014.

the manager and the individual LP and may serve to elevate conduct and mitigation of conflicts to satisfy that obligation, due to privity of contract associated with the side letter, such enhanced investor protections are imputed but not guaranteed to all LPs in the fund.

While its inclusion would strengthen alignment, inserting an ordinary negligence standard among the activities for which the GP is prohibited to self-indemnify may be an untenable standard, used as a pretext for prolonged diligence to zero out risk in prospective deals. Other unintended consequences may include compliance with the rule as justification for exorbitant insurance policies, the premiums for which would be passed on as fund expense or via higher management fees or as the basis for excluding "potentially litigious" LPs from certain funds. Provided the balance of the proposal remains intact – i.e., prohibitions on carving out breach of fiduciary duty, willful misfeasance, bad faith or recklessness – ILPA is amenable to removing "negligence" and substituting instead "gross negligence," with the proviso that the ordinary negligence standard should be applied to material breach of the LPA and side letters. A gross negligence standard in cases of material breach of contract is exceedingly high and illogical, given that no third party can sue the manager for breach of contract, therefore there is no argument for the manager to require LPs to cover the costs of curing the adviser's breach of contract. Prohibiting indemnification of gross negligence would be aligned with the standard under the '40 Act that applies to mutual funds. We would observe that "fiduciary duty" will require more precise jurisdictional definition in the final rule.

ILPA encourages the SEC to clarify that any penalties or disgorgements resulting from an enforcement action that terminates in a settlement, as opposed to a court finding, would be borne by the GP and not indemnifiable.

We acknowledge that managers consider the indemnification and exculpation provisions within the LPA as the necessary to provide comfort required to execute higher risk, higher return investments and understandably deemed essential to the partnership business model. However, the degree to which the standard of loyalty and care have been eroded in the fund documents has shifted the entirety of the risk onto the LPs; determining the standard of care owed to LPs requires recalculating down to the standard of care remaining after subtracting a litany of carveouts in the indemnification and exculpation provisions.

The notion that the proposed minimum standard of care, amended as suggested above, would generate excessive litigation by LPs is a false flag. Given the private markets are predicated on long-term relationships, any LP deemed to be "litigious" would be decidedly unwelcome as an investor in a fund and likely refused an allocation by any manager. There is no evidentiary precedent on which this speculated outcome can be legitimately based. Even in cases of clear breach of the standard of care or loyalty, i.e., fraud, gross negligence, willful misconduct, material breach of the LPA or criminal misconduct, the threshold established within fund documents, often framed as a "final, non-appealable ruling by a court of competent jurisdiction" effectively renders any private right of action that may exist under the relevant jurisdiction to be nearly unattainable in terms of timing and cost to the individual LP.

Certain Non-*Pro Rata* Fee and Expense Allocations

ILPA is generally supportive of this provision, but the SEC should clarify how this rule would impact Separately Managed Accounts (SMAs) and Funds of One. These vehicles can often participate alongside the fund in potential portfolio investments, although this is not always disclosed to investors in the fund. ILPA also encourages the SEC to ensure that the final rule does not impede the commercial speed with which advisers and LPs must act in coinvestment situations and does not suppress the availability of co-investment opportunities.

ILPA encourages the SEC to clarify the impact of this provision on co-investors, specifically for fees and expenses associated with unconsummated deals for co-investors participating as co-underwriters, where there is a differentiated presumption of risk and generally acceptance of some share of costs, versus co-investors who participate on a syndicated basis. Vehicles to house syndicated co-investment capital, as overflow capital to the main fund, may be set up in advance on a no-fee/no-carry basis and generally bear reduced or no expenses; any prohibition to non *pro rata* allocation would require a change to governing documents for such vehicles. For single-asset co-investments, the vehicle is often formed at the time of the consummation of the deal and not in position to absorb a *pro rata* share of broken deal expenses should the deal fall through before the vehicle has been formed. Such vehicles may also involve third party co-investors that are not participating in the commingled fund, making a pure *pro rata* allocation of expenses problematic.[33]

Borrowing (Prohibition on GPs Borrowing from the Fund)

ILPA is supportive of this provision. There is no known scenario where it would be beneficial for an adviser or its related persons to borrow from the fund and no known situations in which a fund would lend a start-up adviser money for the initial costs of fund formation including employee salaries. Sponsors can pursue alternate avenues such as a minority stake sale in the GP to raise startup capital if needed.

ILPA encourages the SEC to be explicit in the definition of “borrowing,” to ensure that existing market practices such as management fee waivers are not unintentionally within scope. While ILPA’s members comprehend that such waivers are often utilized as a means for reducing the sponsor’s tax obligations, there are circumstances in which such waivers are deemed acceptable, such as with newer managers with limited resources to satisfy the sponsor commitment to the fund or in cases where the sponsor commitment is set at a level higher than market norms.

Preferential Treatment

ILPA’s members support complete transparency into the side letter provisions negotiated by all LPs in the same fund, even if they cannot elect those provisions, however, ILPA is concerned that the rule as proposed may have unintended consequences. LPs rely on side letters for statutory, regulatory or legal requirements, without which they would be unable to invest in private funds. ILPA members do not support policy limitations on what provisions may be included in a side letter, or policy limitations on the ability for specific LPs to receive different

[33] ILPA Principles 3.0, Institutional Limited Partners Association, (June 2019) available at: https://ilpa.org/ilpa-principles/

terms to other LPs, based on commitment size or other metrics, in connection with their investment into a private fund, whether in the side letter or other contractual agreement.

ILPA encourages the SEC to narrow the definition of "substantially similar pool of assets" to take into account only vehicles that invest *pari passu* with a private fund. Some LPs invest alongside a private fund in only certain aspects of the fund's strategy, or subject to the investor's consent or veto. Such vehicles should not be considered within the definition of "substantially similar pool of assets."

Prohibition on Preferential Redemption Rights

The SEC should consider limiting the scope of this provision to open-ended funds. Individual investor redemptions are rare in the close-ended fund space. When such redemptions do happen, internal organizational considerations at the investor are normally the reason for such redemptions, not commercial reasons. Investors must retain the ability to redeem in cases where violation of statutes or policies demands, e.g., ERISA or "pay to play" statutes; remedies specified in the side letter may include withdrawal from the fund. Additionally, many investors negotiate for contractual rights that require a private fund adviser to avoid in-kind distributions or to assist those investors with disposing of proposed in-kind distributions. It would be helpful for the Commission to confirm that these sorts of rights are not defined as preferential liquidity in the final rule.

Prohibition on Preferential Disclosure of Certain Portfolio Company Information

ILPA encourages the SEC to clarify that, in the context of preferential portfolio company disclosures, ESG disclosures agreed with individual LPs do not have a material adverse effect on other investors in the fund; costs incurred for providing such reporting, including the use of external specialist consultants, is typically borne by the requesting LPs.

The SEC should consider limiting the scope of this provision to open-ended funds, with exceptions. Selective disclosures in the closed-end fund space do not lead to profits or avoidance of loss of a subset of investors or allow for "front runs."

The SEC should consider the unintended consequence of this proposal in that a universal minimum requirement for portfolio level disclosure would be creating, forcing on individual LPs information beyond that which they currently request, or in a format that may inadvertently expose sensitive commercial information on individual companies within a fund's portfolio in cases where the LP is subject to state-level public records acts requirements that do not exempt such information from public disclosure. Individual LPs subject to such public disclosure legislation will often include language in their side letters stipulating the discretion that the adviser may apply in disclosure of any information deemed sensitive, with appropriate carveouts for information that can never be withheld from an LP. The adviser will typically work with the individual impacted LPs in good faith to establish a means for disclosure that allows the LP to meet their own fiduciary obligations without exposing information to public records request that may violate an NDA or otherwise present commercial risk. A compulsory level of minimum disclosure for portfolio companies for all LPs may violate NDAs with portfolio companies or expose LPs to burdensome bad faith information requests. Additionally, we suggest that in the open-ended fund space, the final rule should not result in walking back on commitments that managers have made to individual investors to provide notice on certain events e.g., key person. Additionally, certain LPs have

portfolio construction and investment monitoring processes predicated on bespoke metrics and algorithms and have therefore negotiated to receive certain information from their private equity advisers on portfolio companies and fund-level performance. ILPA believes that in the closed-end fund context, such bespoke arrangements specific to the format of the information provided to individual LPs does not pose a material, negative impact to other LPs in the fund.

Disclosure of any Preferential Treatment

ILPA seeks in the final rule confirmation from the SEC that institutional LPs would still be able to enter side arrangements with private fund advisers. As such, final requirements for transparency and any prohibitions tied to material, negative impact should be sufficiently clear to the market so as to not provide advisers with a rationale for refusing to grant necessary institution-specific rights via side letters.

Rather than the rolling disclosures proposed in the rule for prospective investors, or annualized disclosures of preferential terms, the SEC should consider an alternative disclosure regime that would provide the requisite transparency for investors in a way that both impacts LP decision making as well as negotiating outcomes. As proposed, the disclosure requirements would be excessively burdensome without yielding decision-useful information for LPs, introducing delays in the negotiating process and additional costs for LPs in fees paid to external LP counsel to review newly issued side letters and engage with the manager on a continuous basis, and potentially impeding the manager's willingness to grant certain terms. Elevating existing industry best practices as a minimum standard may ultimately provide the intended policy solution. We recognize that the negotiating process for closed-end funds differs from that of open-ended funds and encourage the SEC to consider a multi-pronged approach to take those differences into account.

For example, a well-executed most favored nation (MFN) process affords private equity investors with requisite transparency through a compendium provided after the final closing of the fund, by offering investors visibility into the existence and nature of all relevant terms as agreed by investor tier, categorized in a readily digestible way, i.e., with terms categorized by class of investor or specific to regulatory or statutory requirements of individual LPs, coupled with clarity around which provisions are electable versus not based on the size of the LP's commitment, with affiliates of an individual LP being aggregated for the purposes of election. A well-executed process will also include an attestation by the adviser that there are no arrangements under differentiated names with specific LPs that are not disclosed within the compendium. This process reduces administrative burdens on LPs and advisers alike, provides LPs with transparency into all relevant terms agreed upon, provides LPs with the avenue to negotiate for critical terms and can inform LP decision making processes for the current and successive funds. For closed-end funds, we believe a model aligned with the timeliness, completeness and actionability of a best-in-class MFN process would achieve the aims of providing LPs with decision-useful transparency.

Finally, ILPA recognizes that anchor investors, i.e., those participating in the first close, and seed investors, i.e., LPs providing a disproportionate amount of a capital to establish a newer manager, may secure rights that could reasonably be carved out of the MFN process as well as differentiated economics. This differentiated treatment is an accepted market practice by both LPs and advisers and not deemed to harm other investors in the fund. This practice is critical to the health of fundraising and capital formation, encourages/facilitates new entrants to private markets, and helps institutional investors secure the returns they need for their beneficiaries.