



MAPLES
GROUP

ADVANCING FUND GOVERNANCE FOR CLOSED- ENDED STRUCTURES

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Advancing Fund Governance for Closed-Ended Structures

Investors actively participating in the alternative investment fund space cover the full spectrum, from high net worth individuals, funds of funds, life insurance companies and pension plans, through to sovereigns and governments. While some investors are concerned with portfolio diversification by asset, region or sector, others strive for greater balance between assets and liabilities or are motivated by other external factors. The common thread, however, is greater investor sophistication. As the race for alpha has become tighter, investors have been drawn to less liquid strategies, better implemented via closed-ended investment fund structures, which include private equity, private credit, venture capital and real estate, among others.

As the use of these structures has become increasingly prevalent, demand for strong oversight and good governance has grown in tandem. Private equity investors have been at the forefront of efforts to advance governance in the industry. The Institutional Limited Partners Association ("ILPA") has provided detailed guidance on fostering transparency, governance and alignment of interests for general partners ("GPs") and limited partners ("LPs"). Similarly, service providers have played a key role in developing innovative solutions that meet the demands of the industry. As an active participant in the global fund marketplace, the Maples Group has a unique view into best practices and experience supporting some of the world's preeminent institutional investors and private equity managers in implementing the appropriate processes and controls to effectively navigate the complexities of the current environment.

Establishing an Advisory Committee

Increased scrutiny of limited partner advisory committees ("LPACs") and the independence of the GP has resulted in a significant increase in the establishment of advisory or governance committees for private funds over the past five years. While the establishment of an advisory committee is not mandated from a regulatory standpoint and has no authority to act on behalf of or to control the private equity fund, a well-appointed committee can be an important asset to the GP, alongside the traditional LPAC. With advisory committees typically comprised of independent parties who can add real value from a governance perspective, this can bring additional credibility to the GP, particularly for an emerging manager or a smaller fund. The typical responsibilities of advisory committees are outlined in the partnership agreement and generally include voting on change of

control scenarios with respect to the manager or investment valuation matters. Evaluating potential or actual conflicts of interest, along with any other partnership matters raised by the manager and / or advisory board members, is another area where the committee will take an interest. In addition, the committee can answer questions related to ongoing fund operations, as well as accounting and legal matters depending on the particular expertise of its members. Whereas the LPAC is historically comprised of LPs with significant stakes in the limited partnership, these committees represent all investors and can provide considerable benefits to the manager, alongside the LPAC from a fiduciary perspective and in terms of reinforcing the governance structure.

Utilising an Independent General Partner

Limited partnerships, established in Delaware and the Cayman Islands, dominate the private equity landscape. They provide significant flexibility in business structuring for GPs and limited liability for investors, who are removed from day-to-day control and many operational responsibilities. The GP typically has exclusive control over the investments and will delegate certain responsibilities to the manager or advisor and an independent fund administrator.

The use of an independent GP that is not directly affiliated with the manager brings advantages from a governance perspective. A key driver of demonstrating this independence in terms of ownership and control relates to accounting consolidation rules under US GAAP. Holding an equity investment is not the only means by which a sponsor of a closed-ended fund vehicle's GP entity can obtain a controlling financial interest in an entity. If the reporting entity, in this case a private equity fund sponsor, does not have significant influence over the GP vehicle, then it can look past the equity method of accounting for consolidation purposes and instead look to other accounting guidance.

Third Party Independent Valuation

Regulatory change in the industry and the trend towards greater oversight of investment funds have brought robust valuation methodologies into focus. Driven by demands from investors, stakeholders are looking for greater transparency, credibility and consistency in portfolio company valuations. While managers may possess a deep understanding of the intrinsic value of their investments, investors are placing significant importance on valuations by independent parties to provide the assurance they require.

Recently, the SEC has mandated independent reviews of valuation policies and procedures where existing policies are deemed deficient. The Alternative Investment Fund Managers Directive ("AIFMD") in Europe also prescribes an independent valuation process, although it does not require it to be completed by an external valuation specialist. Despite this, many funds still perform their own valuations internally but are increasingly realising the benefits of using independent valuations for portfolio investments, particularly for material or Level III investments.

Independent valuation also helps to alleviate situations where attachment to an investment may impact judgement regarding valuation, especially if the investment is in distress. Private equity firms also often engage valuation specialists to provide additional support including valuation reports for select assets and corroborating internal pricing calculations or models, acting as a "sanity check" for a deal team. The work performed by a third party valuation specialist can generally be incorporated into a framework for robust pricing procedures and is particularly reassuring in instances when managers are looking to raise new funds.

Crucially, comprehensive and well-documented valuation policies and procedures send a strong signal to investors that a manager does not operate in a vacuum but rather uses both internal and external resources to triangulate the best and most appropriate fair value indications. Furthermore, the board or

advisory committee would actively engage with the third party valuator or the investment manager to understand the valuation policy and methodology. This provides investors with additional reassurance that valuations are being approached in a consistent manner.

Professional Directors on the Boards of the General Partner

As with any investment fund structure, professional, independent directors on the boards of GPs can provide numerous advantages to managers and investors alike. Well equipped to provide guidance around the ever-increasing burden of legal and regulatory compliance matters that private equity funds encounter on a daily basis, professional directors can also provide independent oversight of the fund and its service providers that cannot be accomplished on an arm's length basis by a manager.

The general complexity of private equity funds, with inherently more areas where actual or perceived conflicts of interest may exist, highlights the benefit of using professional directors at the GP level. Their independence allows them to govern the fund and avoid potential conflicts around valuation, related party transactions, fees and expenses, to name a few. Conflicts involving the manager and / or one or more LPs, can be better navigated by a majority independent board which can ensure appropriate policies are in place and adhered to. An independent GP board will also make decisions in an acceptable manner, documented accordingly, with transparency and consistency a priority in acting in investors' best interests.

Ultimately, the use of professional directors enables the manager to satisfy investors with a solid governance framework. This simultaneously provides capacity for the manager to deal with issues related to investments and operations. Further, because professional directors have diverse backgrounds and expertise, the right addition to the board can add value for the manager by bringing specific experience or a

different perspective to areas where additional resourcing may be required

Both regulatory requirements and a strong desire from investors for demonstrably higher levels of corporate governance have created a quantum shift in attitudes and behaviour among leading industry participants. While much of this agenda was driven by issues affecting private equity funds that arose from the 2008 financial crisis, including liquidity constraints on funds, as well as a divergence in the interests of limited partners, leading to disputes and ultimately litigation, it remains as relevant as ever given the uncertainty in the market at present. While certain situations may arise amid the more recent market dislocation, private equity managers looking to maximise opportunities in the current environment may take considerable comfort from the quality and expertise of a fiduciary services provider like the Maples Group. We bring an unmatched depth of experience to guide funds through difficult scenarios while upholding the highest standards of corporate governance, particularly as these standards continue to further evolve.

About the Authors

Tammy Jennissen

Tammy is a Senior Vice President within the Maples Group's fiduciary services business, serving as a director to funds for clients across North America. She has expertise with various private equity and hedge fund structures and brings experience in financial services to support clients in addressing complex issues and challenges. She has also authored several articles and participated in numerous industry panels on a variety of governance-related topics. Tammy takes a high-touch, proactive approach and is highly responsive to the funds that she serves, maintaining a commitment to understanding the various aspects of each strategy and staying abreast of legal and regulatory developments. Tammy previously worked for Goldman Sachs (Cayman) Trust Ltd and Deloitte & Touche in Canada and the Cayman Islands.

William Shaw

William is a Senior Vice President within the Maples Group's fiduciary services business, serving a wide range of investment funds including hedge funds, multi-manager funds, private equity funds, unit trusts and segregated portfolio companies, primarily focusing on serving as a director to private equity funds for clients in North America and Asia. William takes a commercial, value-add approach to fund governance and is highly responsive to the funds that he serves. William previously worked for Veronis Suhler Stevenson, a middle-market private equity firm in New York, where as the Controller he focused on the day-to-day operations of several investment vehicles. Prior to that William was an Audit Senior Manager with Ernst & Young. William began his career with Coopers & Lybrand in Boston in 1997.

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Garth is a Vice President within the Maples Group's fiduciary services team, serving a wide range of alternative investment structures, including hedge funds, private equity funds, multi-manager funds, segregated portfolio companies and unit trusts. Previously, Garth worked with the Cayman Islands Monetary Authority as Deputy Head of the Investments Supervision Division. In his role, he led the teams responsible for regulating and overseeing the activities of funds, fund administrators, registered professional directors and securities investment businesses. Prior to this, Garth was an Audit Manager in the alternative investments practice at KPMG in the Cayman Islands and in Canada, where he provided assurance services to investment funds with various investment holdings, strategies and structures, as well as fund administrators, investment managers, trust companies and banks.