FINANCIAL TIMES

July 22, 2015 10:15 pm

US calls for clarity on private equity fees

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Pressure is building on US regulators to improve fee and expenses reporting standards across the private equity industry just weeks after the Securities and Exchange Commission issued an explicit warning to private equity managers to expect more fines for overcharging investors.

A group of senior elected US state officials has written to the SEC calling on the US regulator to ensure that all private equity fees are reported clearly and consistently to investors.

The letter, signed by 13 state treasurers and comptrollers who help to provide oversight of the US public pensions system, said "Greater private equity fee disclosure standards are in the public interest."

The signatories included John Chiang, state treasurer of California, home to the two largest US public pension plans, as well as Scott Stringer and Thomas DiNapoli, the comptrollers who

oversee the large public pension schemes of New York City and New York state respectively.

US public pension funds currently invest around 9.4 per cent of their total assets in private equity. These allocations are expected to grow further over time as private equity managers have delivered better returns than traditional equities and fixed income instruments.

However, the lack of consistent fee disclosure practices by private equity managers combined with the complicated cost structures of private equity vehicles has presented severe difficulties to US public pension schemes that want to provide their members with a complete report of the costs of employing private equity managers.

The letter noted that only management fees paid to private equity managers were regularly disclosed. Other important charges, such as incentive fees, were not reported directly to investors and often appeared only in private equity managers' annual financial statements.

Improving the transparency of all fees paid to private equity managers would strengthen the negotiating position of investors, such as public pension plans, and lead to more efficient investments, said the letter's signatories.

The largest US public pension plan, Calpers, which looks after $300bn in assets on behalf of current and retired state employees in California, is in the process of implementing a new reporting system to better track fees and expenses paid to the managers that run its $30.5bn private equity portfolio.

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Calpers said this month that it would by the autumn be able to report for the first time total "carried interest" or investment profits paid to private equity managers after a three-year work programme.

Only a small minority of US public pension plans currently report carried interest and Calpers initiative could put pressure on other schemes to move towards similar disclosure standards.

Concern among investors over the complexity and opacity of private equity fees has been building for a considerable time. CEM Benchmarking, a Toronto-based consultancy, claimed in a report issued in April that less than half of the very substantial private equity costs incurred by US pension funds were currently being disclosed.

Peter Freire, chief executive of the Institutional Limited Partners Association which represents investors in private equity funds, said current fee disclosures were inconsistent.

“Private equity fees should be disclosed. Clearly this is not happening in every instance and the industry does need to improve,” said Mr Freire.

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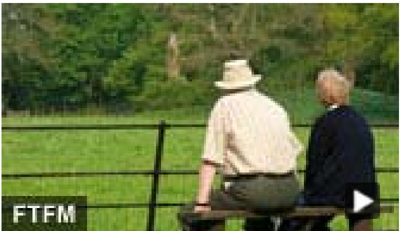

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